Supreme Court, U.S.
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No.

In the Supreme Court of the United States

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC AND PIMCO FUNDS,

Petitioners,

v.

RICHARD HERSHEY, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

In large-scale class actions alleging securities, antitrust, or commodities violations, the class certification determination under Federal Rule of Civil Procedure 23 is typically pivotal because, regardless of the merits of the underlying claims, certification creates an inexorable pressure on defendants to settle given the costs of defending against such actions and the risk of potentially devastating liability. This case involves a class action under the Commodity Exchange Act alleging price manipulation and seeking more than $600 million in damages. The Seventh Circuit upheld the certification of a class that sweeps up numerous plaintiffs who actually benefited from the alleged misconduct, as well as plaintiffs who were on opposite sides of the same trading activity and thus have diametrically opposed interests on how the evidence should be shaped. The questions presented are:

1. Whether or to what extent Rule 23 permits the certification of a class that includes uninjured plaintiffs who actually benefited from the alleged misconduct.

2. Whether or to what extent Rule 23 permits the certification of a class beset by inherent conflicts of interest that affect how the evidence should be shaped.

3. Whether or to what extent a court may certify a class without resolving questions of material fact and finding that plaintiffs have met their burden of proving that each element of Rule 23 is met.

LIST OF PARTIES

1. Petitioner Pacific Investment Management Company, LLC was a defendant in the district court and an appellant in the court of appeals.

2. Petitioner PIMCO Funds was a defendant in the district court and appellant in the court of appeals.

3. Respondents Breakwater Trading LLC and Richard Hershey were plaintiffs in the district court and appellees in the court of appeals.

RULE 29.6 STATEMENT

Pacific Investment Management Company LLC is owned by its employees and Allianz Global Investors of America L.P. Allianz Global Investors of America L.P. is an indirect subsidiary of Allianz AG, a publicly-held company.

PIMCO Funds does not have a parent corporation, and no publicly-held corporation owns 10% or more of PIMCO Funds' stock.

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JURISDICTION

The Seventh Circuit entered its opinion and judgment on July 7, 2009. PIMCO filed a timely petition for panel rehearing or rehearing *en banc* on July 21, 2009. The Seventh Circuit denied PIMCO's petition on July 31, 2009. This Court has jurisdiction under 28 U.S.C. §1254(1).

STATUTORY PROVISIONS INVOLVED

Pertinent statutory provisions are set forth in the appendix hereto. Pet.App.54a-58a.

STATEMENT OF THE CASE

The class action is an important procedural device that both facilitates the litigation of complex cases and presents an enormous potential for abuse. Large-scale class actions alleging securities, antitrust, or commodities violations are a particularly fertile ground for plaintiffs' lawyers seeking to extract huge settlements. Class certification is typically the pivotal event in these cases because, regardless of the merits of the underlying allegations, the certification of a putative class creates an "inordinate or hydraulic pressure on defendants to settle" lest they "bet the company" at trial. *Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 259 F.3d 154, 164 (3d Cir. 2001). This case presents the Court with a timely opportunity to resolve multiple circuit conflicts and provide much needed guidance on the proper procedures and standards for class certification under Rule 23.

At issue is the certification of a class of traders alleging price manipulation under the Commodity Exchange Act ("CEA"), 7 U.S.C. §1 *et seq.* and seeking more than $600 million in damages. The district court certified a class without resolving key factual questions as to whether the inclusion of uninjured plaintiffs in the proposed class or conflicts of interest among class members defeated Rule 23. The Seventh Circuit affirmed, holding that the acknowledged presence of uninjured plaintiffs did not present a problem because *defendants* failed to prove that the "extent" of the overbreadth precluded certification, Pet.App.11a-14a; and that the inherent conflicts of interest among class members on different sides of the *same* trades were merely "hypothetical" and could be addressed later in the case, Pet.App.14a-16a. Like the district court, the Seventh Circuit simply assumed that plaintiffs' bare allegations were sufficient to prove that each element of Rule 23 was met. That decision conflicts with the decisions of this Court and other circuits in several fundamental respects, and warrants plenary review.

The Commodities Futures Market

A futures contract is a promise to deliver a particular quantity of a commodity at a certain price on a certain future date. The party contracting to sell the underlying commodity is said to "sell" the futures contract and is called the "short." *See generally* 1 Philip McBride Johnson & Thomas Lee Hazen, *Derivatives Regulation* §1.02[3] (2004). The party contracting to buy the underlying commodity is said to "buy" the futures contract and is called the "long." *Id.* To satisfy a futures contract, a trader may either deliver or take delivery of the underlying commodity or "offset" or "liquidate" the contract by acquiring an

equal opposing position. *Id.* §§1.02[3]-[4] & n.97. The commodities futures market has been called "volatile and esoteric." *Dunn v. CFTC*, 519 U.S. 465, 468-69 (1997) (internal quotation marks omitted).

Whether a trader realizes a gain or loss on a particular offsetting transaction "depends on the nature of his first contract and the direction in which market prices have moved in the period between the first and second transactions." Johnson & Hazen, *supra*, §1.02[4]. For example, a short trader who later offsets by buying back the position will make money if the contract price has fallen but lose money if the price has risen. "Since every long position comes into being only if there is a countervailing short position (and vice versa) and since one position's gain is necessarily the other position's loss, the gains and losses at any given time net out to zero." *Id.* §1.02[13] n.535.

Statutory Background

Section 9(a) of the CEA makes price manipulation in the commodities markets unlawful. In *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 394-95 (1982), this Court held that the CEA contained an *implied* private right of action but left open its contours. On the heels of *Merrill Lynch*, and in response to this Court's observation that there were potentially significant "interstices" to be filled for the newly created cause of action, *id.*, Congress amended the CEA to include an express private right of action. But Congress explicitly limited that right to individuals who suffered "actual damages" from the alleged CEA violation. Futures Trading Act of 1982, Pub. L. No. 97-444, §235, 96 Stat. 2294, 2322-23 (1983) (codified as amended at 7 U.S.C. §25).

Factual Background

Petitioner PIMCO is an investment management firm that has focused since 1971 on fixed-income investments. PIMCO manages the retirement assets for employees of private and public institutions. PIMCO also manages the bond portfolios of many governments, endowments, charitable entities, corporations and mutual funds, including petitioner PIMCO Funds.[1]

Plaintiffs Breakwater Trading LLC and Richard Hershey ("Plaintiffs") purport to represent a class of investors who established short positions in the June 2005 10-year Treasury note futures contract ("June 2005 Contract" or "the Contract") trading on the Chicago Board of Trade. Plaintiffs claim that PIMCO is responsible for trading losses allegedly suffered when they liquidated short positions at allegedly inflated prices, and seek more than $600 million in damages. Plaintiffs assert that PIMCO artificially increased the price of the Contract from May 9, 2005 to June 30, 2005 ("the class period"). Pet.App.7a.

District Court Proceedings

In August 2005, Plaintiffs filed a class action in the District Court for the Northern District of Illinois, alleging that PIMCO violated Section 9(a) of the CEA

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[1] Petitioner PIMCO Funds is a series of mutual funds that is registered under the Investment Company Act of 1940, 15 U.S.C. §80a-1, *et seq.*, and is governed by its own board of trustees (the majority of whom are not affiliated with PIMCO). As a registered investment company, PIMCO Funds engages PIMCO as its independent investment advisor to manage its pool of assets. Although PIMCO and PIMCO Funds are separate and distinct entities, the arguments presented herein are identical to both, and they are collectively referred to herein as "PIMCO."

by manipulating the price of the Contract. Pet.App. 18a. Plaintiffs sought certification under Rule 23 of a class of "'[a]ll persons who purchased [during the class period] a June 10-year Treasury note futures contract in order to liquidate a short position, or who delivered on the June 2005 futures contract in order to satisfy a short position.'" Pet.App.24a (citation omitted).

The evidence indicated that the proposed class was overbroad and suffered from serious internal conflicts of interest that precluded certification. For example, PIMCO demonstrated that—according to artificiality "ribbons" created by plaintiffs' own experts, purportedly showing fluctuating levels of inflation in the Contract price—a majority of the class members for whom there is trading data in the record actually benefited from the alleged manipulation, making them "net gainers" and therefore unable to show "actual damages" as required to state a claim under the CEA. Pet.App.62a-63a; *see* Seventh Circuit Court of Appeals Separate Appendix of Appellants ("CASA") 206-08, 219-20, 255-71, 340-68, 409-42. Indeed, PIMCO demonstrated that the class is replete with sophisticated institutional traders who switched back and forth between long and short positions throughout the class period, while artificiality (as alleged by plaintiffs' experts) jigged up and down on a daily basis. CASA 124-25, 327-31, 340-68. Accordingly, there are many purported class members who, while they may have liquidated short positions during the class period, actually benefited from the alleged artificiality.

In addition, the trading data in the record showed that class members frequently were on opposite sides of the same trading activity during the relevant period. For example, class representative Hershey held a long

position on days when Breakwater Trading, the other class representative, alleges price artificiality peaked and it suffered damages. CASA 163-65. Similarly, Hershey's long position put him on the opposite side of trading from another class member, Josef Kohen, who initiated and closed a short position at the same time. CASA 164. PIMCO showed that such class members have diametrically opposed interests in characterizing the degree of alleged price artificiality at particular times (or whether there was any artificiality at all), and therefore would have conflicting interests about how the evidence should be shaped, including evidence related to whether there was any wrongful conduct by PIMCO. *See, e.g.*, CASA 129-35, 329-30.

In July 2007, the district court granted Plaintiffs' certification motion. Without resolving these serious factual issues, the court rejected PIMCO's arguments that certification was improper because the defined class included numerous plaintiffs who suffered no economic injury under the loss causation rules recognized in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005),[2] Pet.App.23a-26a, 35a-39a, and because the class was beset by inherent conflicts of interest among class members, Pet.App.33a-35a. Rather, the court simply assumed for purposes of class certification that "all members of the class have suffered injury," Pet.App.26a, and held that, "[a]t this stage of the litigation, it would be premature to deny plaintiffs the opportunity to unify in their task to prove

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[2] In *Dura*, this Court held that whether a plaintiff who has both bought and sold a security at an inflated price has suffered economic loss must be determined by examining *both sides* of his transactions. 544 U.S. at 342-43, 347. As the Seventh Circuit recognized, the same analysis governs here. Pet.App.14a.

that defendants engaged in a common course of conduct that negatively affected all members of the proposed class," Pet.App.25a.

Seventh Circuit Proceedings

After one panel of the Seventh Circuit granted PIMCO's petition for interlocutory review pursuant to Rule 23(f), Pet.App.50a-51a, a different panel of the court affirmed. Pet.App.1a-16a.

The court of appeals recognized that even Plaintiffs acknowledged that the class included traders who actually benefited from the alleged misconduct, Pet.App.7a, and that other courts have held that "it must be reasonably clear at the outset that all class members were injured by the defendant's conduct," Pet.App.10a. But the court concluded that the inclusion of such net gainers did not preclude class certification (or defeat Article III standing, an argument PIMCO never made) "as long as one member of a certified class has a plausible claim to have suffered damages." Pet.App.8a-9a. Moreover, the court assumed, based on the allegations of the complaint, that "plaintiffs sold short, so prima facie at least ... they were injured if the price of cover was artificially inflated during the class period." Pet.App.14a. The court further held that any inquiry into injury should be deferred to "the damages stage of the litigation." Pet.App.7a-8a.

The court observed that, "if the class definition clearly were overbroad, this would be a compelling reason to require that it be narrowed." Pet.App.12a. But the court concluded that "this has not yet been shown." *Id.* In reaching that conclusion, the Seventh Circuit placed on *PIMCO* (*i.e.*, defendants) the burden to prove that the class was overbroad, and suggested

that PIMCO should have sought to "depose a random sample of class members to determine how many were net gainers from the alleged manipulation and therefore were not injured." Pet.App.14a.

The Seventh Circuit also rejected PIMCO's argument that inherent conflicts of interest precluded certification. Pet.App.14a-16a. The court acknowledged that class members would have competing interests in shaping the evidence and, in particular, in calculating and showing artificiality based on when short positions were offset. Pet.App.15a. Rather than requiring the district court to make findings as to whether such conflicts existed, the Seventh Circuit held that, "[a]t this stage in the litigation, the existence of such conflicts is hypothetical." *Id.* The court added that any "real" conflicts could be addressed (if at all) later through use of subclasses. Pet.App.15a-16a.[3]

REASONS FOR GRANTING THE WRIT

Class certification is critical in the high-stakes arena of class litigation alleging federal securities, antitrust, or commodities violations. Because "[a]n order granting certification ... may force a defendant to settle rather than incur the costs of defending a class action and run the risk of potentially ruinous liability," Fed. R. Civ. P. 23 cmt. to 1998 amendments, the gateway requirements of Rule 23 are critical to ensuring that the class action device is not abused. The Seventh Circuit's decision in this case raises several

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[3] On August 5, 2009, PIMCO moved the district court for permission to depose class members to further determine, among other things, how many class members were uninjured. The district court denied that request.

fundamental and interrelated questions on which the lower courts are split concerning the requirements of Rule 23 and the duty of the courts to ensure that those requirements are met *before* certification.

The first question concerns whether or to what extent Rule 23 permits the certification of a putative class that includes plaintiffs who not only were uninjured by, but actually *benefited* from, the alleged misconduct. Until the Seventh Circuit's decision below, "no circuit ha[d] approved of class certification where some class members derive[d] a net economic benefit from the very same conduct alleged to be wrongful." *Valley Drug Co. v. Geneva Pharms., Inc.*, 350 F.3d 1181, 1190 (11th Cir. 2003). Rather, other circuits had barred certification in such circumstances. Moreover, this Court has held that Rule 23 may not be interpreted to "'abridge, enlarge or modify any substantive right,'" *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 613 (1997) (quoting 28 U.S.C. §2072(b)). But that is exactly what happens when Rule 23 is read to permit the certification of a class including numerous plaintiffs who by definition *lack* a cause of action (because they were not injured by the conduct at issue). This issue is recurring and important in antitrust, securities, and commodities class actions given the incentive for plaintiffs to draw classes as big as they can to force lucrative settlements.

The decision below also raises a fundamental and frequently recurring question concerning the scope of Rule 23's adequacy-of-representation requirement and the proper treatment of intra-class conflicts at the certification stage. While the Seventh Circuit acknowledged that the inherent intra-class conflicts among class members on different sides of the same

transactions gave class members opposing interests in how the evidence should be shaped, the court held that those conflicts did not preclude certification on the ground that the conflicts were merely "hypothetical" at this time and could be addressed at some later point. Pet.App.15a-16a. That holding conflicts with this Court's decisions (*e.g.*, *Amchem*) stressing the importance of Rule 23's adequacy-of-representation requirement, and with decisions of other circuits holding that analogous conflicts precluded certification.

And the Seventh Circuit's resolution of these issues raises a recurring and over-arching question concerning the procedures governing the Rule 23 determination. The court approved class certification even though the evidence, at a minimum, raised serious questions about whether the class was overbroad or beset by intra-class conflicts. In doing so, the court simply assumed (despite the contrary evidence) the truth of plaintiffs' allegations on class injury and deferred any factual inquiry into the degree of intra-class conflicts until a later day. Moreover, the court placed on *defendants* the burden of proving that the requirements of Rule 23 were not met. That decision conflicts with the decisions of other circuits holding that courts must ensure that the record in fact supports each Rule 23 requirement *before* certification (informed by evidentiary proceedings and discovery, if necessary), and that plaintiffs bear the burden of proving that the requirements of Rule 23 are met.

Certiorari is warranted to resolve these conflicts of authority, to provide guidance to lower courts, and to ensure the faithful application of Rule 23 to the class certification decision. The decision below is already being invoked by lower courts and class action

plaintiffs to support certification of ever more adventurous and bloated classes. And if, as the Seventh Circuit held, *this* class on *this* record satisfies Rule 23, then only the rare antitrust, securities, or commodities class will flunk Rule 23. Such a radical and unsettling revision of Rule 23's gateway requirements warrants this Court's review.

I. CERTIORARI IS WARRANTED TO REVIEW THE SEVENTH CIRCUIT'S DECISION THAT THE INCLUSION OF NUMEROUS UNINJURED PLAINTIFFS DOES NOT PRECLUDE CLASS CERTIFICATION

The Seventh Circuit held that certification was warranted even though the record indicated that the defined class includes numerous plaintiffs who not only were uninjured by the conduct at issue, but actually benefited from that conduct. That decision directly conflicts with the decisions of this Court and other circuits on both the substantive requirements of Rule 23 and the inquiry demanded before a class is certified.

A. The Decision Below Conflicts With The Decisions Of Other Circuits Holding That Certification Of Such An Overbroad Class Is Improper

1. The certified class at issue undeniably includes numerous plaintiffs who actually benefited from any distortion in futures pricing. The extremely active trading patterns in this market, and the erratic fluctuations in the artificiality alleged by plaintiffs, make it inevitable that the alleged misconduct, if true, produced winners as well as losers—including among those who sold short. Indeed, at the time of certification, a majority of class member traders/

accounts for whom trading data is in the record were net gainers according to plaintiffs' own experts. Class representative Hershey, for example, engaged in three transactions during the Class Period: two purchases on May 11, 2005 (one of which closed out a pre-existing short position) and a sale on May 27, 2005 to liquidate his remaining long position. CASA 206-08, 219-20. Based on Plaintiffs' own artificiality ribbons, these trades netted an economic gain for Hershey from the alleged artificiality. The same goes for other class members, including large institutional investors that engaged in many trades daily. CASA 255-71, 340-68.

2. The Seventh Circuit acknowledged that "some of the class members probably were net gainers from the alleged manipulation," Pet.App.12a, but held that class certification was proper. That decision directly conflicts with the decisions of other circuits. Indeed, until the decision below, "no circuit ha[d] approved of class certification where some class members derive[d] a net economic benefit from the very same conduct alleged to be wrongful by the named representatives of the class." *Valley Drug Co. v. Geneva Pharms., Inc.*, 350 F.3d 1181, 1190 (11th Cir. 2003); *see also Allied Orthopedic Appliances, Inc. v. Tyco Healthcare Group L.P.*, 247 F.R.D. 156, 177 (C.D. Cal. 2007) ("[N]o circuit approves of class certification where some class members derive a net economic benefit from the very same conduct alleged to be wrongful by the named representatives of the class, let alone where some *named* plaintiffs derive such a benefit.").

Pickett v. Iowa Beef Processors, 209 F.3d 1276 (11th Cir. 2000)—which the Seventh Circuit recognized, but declined to follow, Pet.App.15a—illustrates the approach taken by other circuits. That case involved a

class action alleging price manipulation in the market for cattle. 209 F.3d at 1277-78. As the Eleventh Circuit recognized, however, the defined class at issue "include[d] those who claim harm from the very same acts from which other members of the class *have benefitted* [*sic*]." *Id.* at 1280 (emphasis added). The Eleventh Circuit therefore reversed the district court's certification order, holding that "a class cannot be certified ... when it consists of members who benefit from the same acts alleged to be harmful to other members of the class." *Id.* As the court explained, such a "plaintiff class cannot satisfy the adequacy requirement of Rule 23(a)(4)." *Id.*

Likewise, in *Phillips v. Klassen*, 502 F.2d 362, 367-68 (D.C. Cir.), *cert. denied*, 419 U.S. 996 (1974), the D.C. Circuit held that a class of retired government employees could not maintain a class action for coerced retirement where some members of the class gained from the alleged wrongdoing. As the court explained, "[w]hen, as here, there is complaint as to injury from an allegedly invalid action of a Government official and the action may be taken as *conferring economic benefits* or working economic harm, depending on the circumstances of the individual, the foundations of maintenance of a class action are undermined." *Id.* at 367 (emphasis added). Because there would be "divergent views among the" plaintiff class "as to whether they have been injured or benefited," the court affirmed the denial of class certification. *Id.*

Other circuits also have held that Rule 23(b)(3)'s predominance requirement cannot be met where it is apparent at the certification stage that the class includes both injured and uninjured members. For example, in *Newton v. Merrill Lynch, Pierce, Fenner &*

Smith, Inc., 259 F.3d 154 (3d Cir. 2001), the Third Circuit held that certification of a class of securities traders was improper where plaintiffs' claims required "an economic injury determination for each trade" to determine "whether securities violations occurred." *Id.* at 190. Like the alleged price manipulation here, the trading at issue in *Newton* "did not necessarily injure each class member," so some members suffered economic injury and others did not. *Id.* at 187.

In *In re Hydrogen Peroxide Antitrust Litigation*, 552 F.3d 305, 311-12 (3d Cir. 2009), the Third Circuit similarly recognized that proof of injury "often is critically important" in large-scale class actions, and held that plaintiffs must demonstrate at class certification that the fact of injury "is capable of proof at trial through evidence that is common to the class rather than individual to its members." Rejecting the notion that class certification required plaintiffs to make only "'a threshold showing that the element of impact [*i.e.*, fact of damage] will predominantly involve generalized issues of proof,'" *id.* at 321 (citation omitted), Chief Judge Scirica explained for the court that Rule 23 requires "a careful, fact-based approach, informed, if necessary by discovery," *id.* at 326, and vacated the district court's class certification order.

And, in *Bell Atlantic Corp. v. AT&T Corp.*, the Fifth Circuit held that two classes of plaintiffs alleging harm "by the refusal of [AT&T] to permit the passage of caller identification ... data across its long-distance telephone network" did not satisfy Rule 23(b)(3)'s predominance requirement. 339 F.3d 294, 296 (5th Cir. 2003). "Establishing causation, or 'fact of damage', requires the plaintiff to demonstrate a causal connection between the specific antitrust violation at

issue and an injury to the business or property of the antitrust plaintiff." *Id.* at 302. The Fifth Circuit held that such a showing could not be made—despite the plaintiffs' proposed "formula" to calculate damages—because "[t]he record indicates that ... any adequate estimation of actual damages suffered would require" "individualized inquiries." *Id.* at 304-07.

The Seventh Circuit's decision in this case cannot be reconciled with these holdings. The undisputed fact that "some of the class members probably were net gainers," Pet.App.12a, directly impacts the Rule 23(b)(3) determination because it means that the fact of injury—an essential element of the CEA cause of action—must be established on an individualized trade-by-trade basis, as in *Newton*. And by glossing over this defect, the Seventh Circuit failed to require that "a careful, fact-based approach, informed, if necessary by discovery," *Hydrogen Peroxide*, 552 F.3d at 326, was undertaken to ensure that Rule 23 was satisfied.

B. The Decision Below Conflicts With This Court's Decisions Recognizing That Rule 23 May Not Be Used To Expand Substantive Rights

The Seventh Circuit's decision upholding the certification of the overbroad class here conflicts with this Court's decisions as well. In *Amchem Products, Inc. v. Windsor*, 521 U.S. 591 (1997), the Court stressed that "Rule 23's requirements must be interpreted in keeping ... with the Rules Enabling Act, which instructs that rules of procedure 'shall not abridge, enlarge or modify any substantive right.'" *Id.* at 613 (quoting 28 U.S.C. §2072(b)); *see also id.* at 629; *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 845 (1999) ("[N]o reading of [Rule 23] can ignore the Act's mandate that

'rules of procedure "shall not abridge, enlarge or modify any substantive right."'") (quoting *Amchem*, 521 U.S. at 613). The Seventh Circuit flouted that mandate in upholding certification of the class at issue.

The CEA's express private right of action extends only to those who have suffered "actual damages" from the alleged manipulation. 7 U.S.C. §25(a)(1). "[A]ctual damages' is therefore an essential element of the cause of action. *See, e.g., Damato v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 878 F. Supp. 1156, 1160-61 (N.D. Ill. 1995); *Kolbeck v. LIT Am., Inc.*, 923 F. Supp. 557, 566-67 (S.D.N.Y. 1996); *Three Crown Ltd. P'ship v. Caxton Corp.*, 817 F. Supp. 1033, 1042 & n.14 (S.D.N.Y. 1993). Indeed, as noted, Congress added the "actual damages" element of the CEA precisely to *limit* the scope of the cause of action. Plaintiffs who cannot show "actual damages" lack a private right of action—and therefore lack "statutory standing," *see Warth v. Seldin*, 422 U.S. 490, 500 (1975)—under the CEA.

Certifying a class of uninjured CEA plaintiffs contravenes this Court's decisions, the Rules Enabling Act, and Rule 23 by enlarging the substantive rights of these class members. That is not a mere "damages" issue, as the Seventh Circuit held, Pet.App.7a-8a; it goes to the availability of the cause of action *vel non*. *See Hydrogen Peroxide*, 552 F.3d at 311 ("'Proof of injury ... must be distinguished from calculation of damages.'") (citation omitted); *Newton*, 259 F.3d at 189 (establishing economic loss goes *not* to "the calculation of damages but whether or not class members have any claims at all"); *Windham v. Am. Brands, Inc.*, 565 F.2d 59, 66 (4th Cir. 1977) (presuming class-wide proof of injury in an antitrust class action would "contravene the mandate of the Rules Enabling Act"), *cert. denied*,

435 U.S. 968 (1978). The fact that the Seventh Circuit sanctioned a result forbidden by this Court's decisions is reason enough to grant review.

C. The Decision Below Conflicts With The Decisions Of This Court And Other Circuits On The Inquiry Demanded Before Certification

The Seventh Circuit compounded its errors and exacerbated the circuit conflict by concluding that the record was sufficient to support certification and by placing on defendants the burden to show that certification was improper. Pet.App.12a-14a.

1. In *General Telephone Co. of the Southwest v. Falcon*, 457 U.S. 147, 161 (1982), the Court held that a class "may only be certified if the trial court is satisfied, after a rigorous analysis, that the prerequisites of Rule 23(a) have been satisfied." As illustrated by the decision below, in the 25 years since *General Telephone*, the lower courts have developed conflicting standards on what that "rigorous analysis" should entail. *See Loftin v. Bande (In re Flag Telecom Holdings Ltd. Sec. Litig.)*, 574 F.3d 29, 39-40 (2d Cir. 2009) (discussing different approaches); *Brown v. Am. Honda (In re New Motor Vehicles Canadian Export Antitrust Litig.)*, 522 F.3d 6, 25-26 (1st Cir. 2008).

The Seventh Circuit's decision upholding certification on the record here conflicts with the decisions of other circuits holding that "the decision to certify a class calls for findings by the court, not merely a 'threshold showing' by a party, that each requirement of Rule 23 is met," and that "[f]actual determinations supporting Rule 23 findings must be made by a preponderance of the evidence." *Hydrogen Peroxide*, 552 F.3d at 307; *see Miles v. Merrill Lynch & Co. (In re*

Initial Pub. Offering Sec. Litig.), 471 F.3d 24, 41 (2d Cir. 2006) (Certification is not appropriate unless a court "receive[s] enough evidence, by affidavits, documents, or testimony, to be satisfied that each Rule 23 requirement has been met."); *see also Flag Telecom*, 574 F.3d at 38 ("[L]ower courts have an 'obligation' to resolve factual disputes relevant to the Rule 23 requirements, and to determine whether the requirements are met ...."); *Oscar Private Equity Invs. v. Allegiance Telecom, Inc.*, 487 F.3d 261, 266-68 (5th Cir. 2007) (plaintiff has burden of proving loss causation at certification stage to establish that predominance requirement is met); *Gariety v. Grant Thornton, LLP*, 368 F.3d 356, 365 (4th Cir. 2004).[4]

As Chief Judge Scirica explained for the court in *Hydrogen Peroxide*, "the requirements set out in Rule

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[4] *In re IPO* alone illustrates how the standards for class certification have perplexed the lower courts. In *In re IPO*, the Second Circuit carefully reconsidered and distanced itself from earlier cases upholding class certification, including *Wal-Mart Stores, Inc. v. Visa U.S.A. Inc. (In re Visa Check/MasterMoney Antitrust Litig.)*, 280 F.3d 124, 139-40 (2d Cir. 2001), *cert. denied*, 536 U.S. 917 (2002). In *Szabo v. Bridgeport Machines, Inc.*, 249 F.3d 672, 676 (7th Cir. 2001), the Seventh Circuit observed that, "[b]efore deciding whether to allow a case to proceed as a class action, ... a judge should make whatever factual and legal inquiries are necessary under Rule 23." In contrast to the decisions of other circuits (*e.g.*, *In re IPO* and *Hydrogen Peroxide*), however, *Szabo* provided no guidance as to *what* "factual and legal inquiries" are "necessary under Rule 23" and, instead, left this determination almost entirely up to the district judge. *Id.* at 676-77. As a result, both the district court in this case (which recognized *Szabo*, Pet.App.27a) and the Seventh Circuit (which saw no need even to mention *Szabo*) concluded—in conflict with the decisions of other circuits—that the record supported certification without resolving the disputed facts concerning the degree of overbreadth and intra-class conflicts.

23 are not mere pleading rules." 552 F.3d at 316. Therefore, courts must go beyond the pleadings and engage the facts through discovery and evidentiary proceedings in order to ensure that certification is proper. *See id.* at 316-21. That approach takes into account the touchstone significance of the certification decision on the course of class litigation, as well as recent amendments to Rule 23. *See id.* at 310, 318-19.

The decision below is the antithesis of the approach mandated by other circuits to protect against off-the-cuff class certifications. Indeed, rather than ensuring that plaintiffs had established each element of Rule 23 by a preponderance of the evidence before the class was certified, the Seventh Circuit simply speculated that there were "probably" not so "many" net gainers as to preclude certification. Pet.App.12a. And to generate the premises for that speculation, the Seventh Circuit assumed that plaintiffs' ultimate allegations of price manipulation were true, an approach rejected in the cases cited above.[5] Armchair

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[5] The Seventh Circuit reasoned that there were "probably not many" class members who were net long because in the absence of "a great many net short sellers ... PIMCO could not have driven its price to an artificially high level." Pet.App.13a. But that erroneously equates net gainers with traders who were net long and impermissibly accepts Plaintiffs' ultimate allegations of price manipulation. Likewise, the Seventh Circuit assumed that any net gainers would have to be both short (to be in the class) and long (to benefit from the alleged manipulation), that any such traders must have been pursuing hedging strategies, and that traders rarely hedge their positions *completely*. Pet.App.12a-13a. But that reasoning ignores the fact that the market includes commodities traders who frequently switch back and forth between net long and net short—not to "hedge," but to "speculate." Robert W. Kolb & James A. Overdahl, *Understanding Futures Markets* 154-57 (6th ed. 2006). Class

economics and naked assumptions about the plaintiffs' theory of the case or the likely members of a class are no substitute for the factual findings required before a court may certify a class under Rule 23.

2. Rather than recognizing that plaintiffs had failed to meet their burden in proving that each requirement of Rule 23 was met, the Seventh Circuit flipped the burden onto defendants and held that certification was warranted because *defendants* had not "depose[d] a random sample of class members to determine how many were net gainers from the alleged manipulation." Pet.App.14a. That holding also conflicts with the decisions of this Court and other circuits.

In *Amchem*, this Court held that "parties seeking class certification must show that the action is maintainable under Rule [23]." 521 U.S. at 614. Other circuits have recognized and applied that rule. *See, e.g.*, *Valley Drug Co.*, 350 F.3d at 1196 ("[U]nder Rule 23 it is the plaintiffs, as the moving party, who bear the burden of proving that class certification is appropriate."); *Hydrogen Peroxide*, 552 F.3d at 315-16 ("[I]t is clear that the party seeking certification must convince the district court that the requirements of Rule 23 are met ...."); *In re Am. Med. Sys., Inc.*, 75 F.3d 1069, 1086 (6th Cir. 1996) (reversing where district court had "ordered defendants to 'show cause

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representative Hershey, for example, switched from being short to long and benefited more from the alleged artificiality on his long position than he lost on his short position. And trading data showed institutional traders who engaged in numerous trades daily (short and long) to exploit market conditions. Regardless, class members did not benefit from the alleged artificiality only on long positions. The erratically fluctuating artificiality alleged by plaintiffs would have benefited many *short* positions as well.

why [the court] shouldn't certify a class,'" thereby "plac[ing] the burden on defendants to disprove plaintiffs' 'entitlement' to class certification"); *accord Flag Telecom*, 574 F.3d at 39-40; *Lozano v. AT&T Wireless Servs., Inc.*, 504 F.3d 718, 724 (9th Cir. 2007); *Richards v. Delta Air Lines, Inc.*, 453 F.3d 525, 529 (D.C. Cir. 2006); *Bell Atl. Corp.*, 339 F.3d 294, 301 (5th Cir. 2003).

The Seventh Circuit's decision upholding class certification on the ground that *defendants* failed to prove "the extent to which" the defined class is overbroad, Pet.App.13a (emphasis added), turns the required burden of proof on its head. It was *Plaintiffs'* burden to prove that the defined class—despite its obvious structural flaws—meets the requirements of Rule 23. To satisfy that burden, Plaintiffs were obligated to present evidence showing that the class was *not* overbroad. The Seventh Circuit's contrary ruling is seriously misguided and warrants review. Indeed, putting the burden on defendants was particularly inappropriate on this record, which showed that a majority of the plaintiffs for whom there was trading data, including named plaintiff Hershey (who plaintiffs presumably thought had among the strongest claims), had no net loss. If anything, such a record justifies giving Plaintiffs' evidence closer scrutiny.

II. CERTIORARI IS WARRANTED TO REVIEW THE SEVENTH CIRCUIT'S DECISION THAT THE INHERENT CONFLICTS OF INTEREST DO NOT PRECLUDE CERTIFICATION

Certiorari is also warranted to review the Seventh Circuit's decision that class certification was proper despite the evidence that class members were on

opposite sides of the same transactions and therefore had diametrically opposed interests on how the evidence should be shaped. That decision conflicts with the decisions of this Court and other circuits on the demands of Rule 23's adequacy-of-representation requirement and exacerbates a conflict over the extent to which a court is required to scrutinize the severity of such intra-class conflicts *before* certification.

A. The Decision Below Conflicts With The Decisions Of This Court And Other Circuits On The Basic Requirements Of Rule 23(a)(4)

1. The class at issue is defined to include *any* trader who liquidated a short position during the class period, regardless of when the trader established the short position or offset or liquidated that position and regardless of the trader's other transactions during the class period. The defined class thus crudely sweeps up large institutional traders who were net long at various times during the class period with traders who were net short, and even traders who purchased and sold *on opposite sides of the same transactions*.

Because each class member's showing of injury will depend on establishing that any artificial inflation in the price was lower when *they* sold short than when *they* bought to liquidate the short position, individual class members have diametrically opposed interests in how the evidence should be shaped and, in particular, how the artificiality curve is defined. Class members who offset the bulk of their short positions early in the class period and were predominantly long or neutral thereafter would want to show that the alleged "inflation" in the price peaked early, and that the later increases in price were "due to market forces for which

PIMCO was not responsible." Pet.App.15a. Class members who were predominantly short later in the period would want to prove the opposite. And at the level of specific transactions, class members who bought at a particular time would want to maximize the calculation of artificiality, while class members who sold would want to minimize it.[6]

These conflicts are not merely "hypothetical," *id.*, but are actual and already inflicting harm. Plaintiffs presented their theories and evidence about the fluctuations of alleged price artificiality through the artificiality "ribbons" constructed by their experts before the certification decision. Pet.App.62a-63a. The class representatives thus have already committed to a position on this central issue on which the interests of class members conflict, and as a result some class members already have been prejudiced. The contradictory outcomes generated by applying the differing "ribbons" propounded by plaintiffs' own experts to identical trading patterns underscore this conflict. *See, e.g., id.*; CASA 219-20, 337, 340-68, 370.

The only thing not known at this point is *which* class members fall into the opposing camps. The essence of the Seventh Circuit's holding, therefore, is that the obvious prejudice to some class members can be ignored at class certification—notwithstanding Rule 23(a)(4)'s adequacy-of-representation requirement—so

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[6] For example, class representative Hershey held a long position when Breakwater Trading, the other class representative, alleges price artificiality peaked and it suffered damages. CASA 163-65. Similarly, Hershey's long position put him on the opposite side of trading from another class member, Josef Kohen, who initiated and closed a short position at the same time. CASA 164.

long as we do not know who they are. In other words, under the Seventh Circuit's decision, a "potential" conflict does not become "actual" until it is clear precisely whose ox is being gored.

2. In *Amchem*, this Court explained that "[t]he adequacy inquiry under Rule 23(a)(4) serves to uncover conflicts of interest between named parties and the class they seek to represent." 521 U.S. at 625. The Court then held that the obvious conflicts of interests among a settlement class of "current and future asbestos-related claims" precluded certification. *Id.* at 597, 627-28. As the Court explained, the "critical goal" of the "currently injured" class members was to obtain "generous immediate payments," whereas the goal of the "exposure-only plaintiffs" was to "ensur[e] an ample, inflation-protected fund for the future." *Id.* at 626. The conflict of interest is at least as strong here, where, as explained above, class members are on opposite sides of the same trades and have diametrically opposed interests in characterizing the degree of alleged price artificiality at particular times.[7]

The Seventh Circuit's decision also conflicts with the decisions of other circuits. For example, in *Langbecker v. Electronic Data Systems Corp.*, 476 F.3d 299, 315-16 (5th Cir. 2007), the Fifth Circuit held that a class of 401(k) investors could not be certified because class members had pursued different trading strategies

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[7] The Seventh Circuit's decision also conflicts with this Court's decision in *East Texas Motor Freight System, Inc. v. Rodriguez*, 431 U.S. 395, 403 (1977). In that case, the Court held that individuals who "could have suffered no injury as a result of [the conduct at issue]" were "simply not eligible to represent a class of persons who did allegedly suffer injury." *Id.* at 403-04. As explained, class representative Hershey was not injured.

and therefore had different interests in shaping the evidence. The Fifth Circuit explained that the class members "were affected by the drop in price in dramatically different ways," with some class members profiting and some losing money. *Id.* at 315. The same goes here, where class members were on opposite sides of the same trades on the same day—some experiencing a loss and others a net gain, depending on how artificiality is characterized.

Valley Drug, 350 F.3d at 1184-86—which the Seventh Circuit recognized, but declined to follow, Pet.App.14a—is to the same effect. That case involved an antitrust class action attacking the delay in the introduction of a drug into the market. Numerous members "of the certified class arguably experienced a net gain from the conduct alleged to be illegal by the named representatives." 350 F.3d at 1188. The court held that "[a] fundamental conflict exists where some members claim to have been harmed by the same conduct that benefited other members of the class." *Id.* at 1189. Despite undeniable evidence of the same kind of "fundamental conflict" here, the Seventh Circuit upheld class certification and called PIMCO's objections "ill conceived." Pet.App.16a.

B. The Decision Below Exacerbates The Conflict Among The Lower Courts On The Duty to Address Conflicts Before Certification

1. Instead of holding that such obvious conflicts of interest among class members precluded certification, the Seventh Circuit upheld certification and observed that, "[i]f and when" the conflicts "become real, the district court can certify subclasses with separate representation of each." Pet.App.15a. But as

discussed, the conflicts here already are "real." And, more to the point, the Seventh Circuit's conclusion that certification was warranted without any evidentiary inquiry at this stage into the severity of the conflicts of interest splits with the decisions of other circuits.

Many large-scale securities, commodities, and antitrust class actions involve intra-class conflicts of some kind. Nonetheless, there can be material differences in both the degree and kind of conflicts that may exist. For example, a securities class action may be dominated by "buy and hold" investors. "In and out" traders may be rare, and short sellers excluded entirely. The alleged price "artificiality" often is created by a misrepresentation and then remains constant or moves only in one direction, until it is dispelled by a corrective disclosure. In those circumstances, the class is more likely to share a basic unity of interest, even if some of their interests conflict on relatively minor matters. And if subclasses are needed, they often can be defined by a few simple, objective criteria—such as those who purchased before or after a particular corrective disclosure.

Here, by contrast, the class includes sophisticated institutional traders who switched back and forth between long and short positions throughout the class period, often taking positions opposite each other at the same times while the artificiality ribbons (as alleged by Plaintiffs' experts) went up and down on a daily basis. Pet.App.62a-63a; CASA 340-68. In such a purported class, there is no predictable unity of interest or adequacy of representation—only chaos, and an opportunity for class counsel to earn a windfall by settling the claims of hundreds of class members whose actual interests vary greatly.

2. Despite the importance of such distinctions, the lower courts have taken widely divergent approaches to investigating conflicts issues at the certification stage. Consistent with the teachings of this Court's decisions and the circuit cases discussed above, some courts have recognized that the severity of intra-class conflicts of interest must be tested *before* certification. For example, in *Valley Drug* the Eleventh Circuit admonished that "we do not believe that it is unduly burdensome to require the named representatives to bring forth evidence to the court that no fundamental conflict exists among the class members, especially in view of the fact that under Rule 23 it is the plaintiffs, as the moving party, who bear the burden of proving that class certification is appropriate." 350 F.3d at 1196. That approach squares with the circuits that have held that "the district judge must receive enough evidence ... to be satisfied that each Rule 23 requirement has been met"—*before* certifying a class. *In re IPO*, 471 F.3d at 41; *see* pp. 17-18, *supra*. In stark contrast, the Seventh Circuit relieved plaintiffs of their burden to bring forth *evidence* that "no fundamental conflict exists" and held that testing the conflicts now "would be premature." Pet.App.16a.

This conflict is entrenched in the district courts, whose class certification decisions are often not reviewed at the circuit level because of settlements. In *In re Seagate Technology II Securities Litigation*, 843 F. Supp. 1341, 1359 (N.D. Cal. 1994), Judge Walker refused to defer consideration of the intra-class conflicts presented by a putative securities class including traders who purchased *and sold* during the class period ("in/out traders"). As the court explained, such a conflict "presents not only an *eventual* problem

with the damages element, but also an *immediate* problem" as to the development of evidence. *Id.* at 1358-59. Moreover, the court explained, subclasses are often not a realistic solution to conflicts in price manipulation cases where the alleged artificiality and trading patterns are complex, because of the prospect of an unmanageable number of subclasses. *Id.* at 1361-62. Accordingly, the court held that "the precise composition of the plaintiff class, and the resultant extent and severity of class conflicts, are factual inquiries which must be made [before certification] on a case-by-case basis." *Id.* at 1365. Judge Walker further suggested that a court armed with a real factual understanding of the structure of the class could then seek to strike a sensible balance between conflicts issues and the utility of the class action device—for example narrowing the class to minimize conflicts problems when that could be done at acceptable cost to other jurisprudential interests.

Seagate's analysis has been expressly adopted by several lower courts that have refused to certify classes beset by conflicts of interest analogous to the ones here. *See, e.g., In re Physician Corp. of Am. Sec. Litig.*, No. 97-3678-CIV, 2003 WL 25820056, at *10 (S.D. Fla. May 21, 2003); *Ziemack v. Centel Corp.*, 163 F.R.D. 530, 542 (N.D. Ill. 1995); *Ballan v. Upjohn Co.*, 159 F.R.D. 473, 485-86 (W.D. Mich. 1994). Other courts have simply refused to certify classes because of such conflicts in similar cases without explicitly citing *Seagate*. *See, e.g., Premium Plus Partners, L.P. v. Davis*, No. 04 C 1851, 2008 WL 3978340, at *4-6 (N.D. Ill. Aug. 22, 2008); *Centurions v. Ferruzzi Trading Int'l, S.A.*, No. 89 C 7009, 1994 WL 114860, at *9-17 (N.D. Ill. Jan. 7, 1993); *McCullough v. Ferruzzi*

Trading Int'l, No. 90 C 1138, 1993 WL 795256, at *4-5 (N.D. Ill. Jan. 7, 1993).

Other lower courts, however, have assumed that intra-class conflicts can be managed later by defining sub-classes, or by severing the trial into separate liability and "damages" phases. Most of these decisions, like the Seventh Circuit's here, improperly seek to side-step the issue of conflicts under Rule 23(a)(4) entirely, by deeming it somehow "premature," or relevant only to the determination of damages. *See, e.g., In re Scientific-Atlanta, Inc. Sec. Litig.*, 571 F. Supp. 2d 1315, 1335 (N.D. Ga. 2007); *Tracinda Corp. v. DaimlerChrysler AG (In re DaimlerChrysler AG Sec. Litig.)*, 216 F.R.D. 291, 297 (D. Del. 2003); *In re Gaming Lottery Sec. Litig.*, 58 F. Supp. 2d 62, 69-71 (S.D.N.Y. 1999); *Weikel v. Tower Semiconductor Ltd.*, 183 F.R.D. 377, 394-95 (D.N.J. 1998). And like the decision below, most of these decisions simply hold out the prospect of subclasses down the road as a means of deferring the conflicts issue, without any meaningful analysis of whether subclasses would be practical. *E.g., Scientific-Atlanta*, 571 F. Supp. 2d at 1335; *Tracinda Corp.*, 216 F.R.D. at 297. Because certification often forces settlement of class actions, that assumption is rarely tested in the crucible of actual trial management, or reviewed on appeal.

The conflicts-of-interest problem is pervasive in large-scale class actions such as this and frequently litigated, yet the lower courts are divided about whether and to what extent such conflicts must be tested at the certification stage under Rule 23. And this division underscores the broader question of the duty of the courts to ensure that the record supports each requirement of Rule 23 before certifying a class.

Particularly given the stark intra-class conflicts discussed above, this case presents an ideal vehicle for the Court to provide guidance on these questions.

III. THE QUESTIONS PRESENTED ARE EXCEPTIONALLY IMPORTANT

"[T]he fight over class certification is often the whole ball game" in class action litigation, given the "high stakes involved in class certification decisions" for defendants as well as plaintiffs. *Hartford Accident & Indem. Co. v. Beaver*, 466 F.3d 1289, 1294 (11th Cir. 2006). As a result, "[f]ew pretrial motions in our civil justice system elicit as much controversy as those for the certification of class actions." Richard A. Nagareda, *Class Certification in the Age of Aggregate Proof*, 84 N.Y.U. L. Rev. 97, 97 (2009). In large-scale securities, antitrust, and commodities class actions, the certification fight often turns on whether the defined class is overbroad because of the inclusion of uninjured plaintiffs, and whether conflicts of interest among class members preclude certification. And the burden of proof and evidentiary requirements at certification are often dispositive. Given the touchstone importance of the certification determination, the proper resolution of the questions presented is key to ensuring that the class action procedure is not abused.

As this Court has recognized, "class action practice has become ever more 'adventuresome'" in the decades since Rule 23 was adopted. *Amchem*, 521 U.S. at 617. Antitrust, securities, and commodities class actions have long been a particularly fertile ground for plaintiffs' lawyers, because of the lucrative settlements they frequently yield irrespective of the merits of the

claims.[8] In practice, "[a]lmost all *certified* class actions settle." Thomas E. Willging & Shannon R. Wheatman, Federal Judicial Center, *An Empirical Examination of Attorneys' Choice of Forum in Class Action Litigation* 48 (2005). The amount of money spent each year in settling these class actions is enormous. In 2007, for example, the average settlement value of securities class actions was $62.7 million. Ellen M. Ryan & Laura E. Simmons, Cornerstone Research, *Securities Class Action Settlements, 2009 Review and Analysis* 2, *available at* http://securities.stanford.edu/Settlements/REVIEW_1995-2008/Settlements_Through_12_2008.pdf. From 1996 through 2007, defendants spent $53.6 billion settling securities class actions. *Id.* As a result, as one commentator has observed, large-scale class actions "have more in common with business deals than they do with traditional adversarial litigation," making the courthouse a "site for large financial transactions." William B. Rubenstein, *A Transactional Model of Adjudication*, 89 Geo. L.J. 371, 372 (2001).

This phenomenon is not new. "Judge Friendly, who was not given to hyperbole, called settlements induced by a small probability of an immense judgment in a class action 'blackmail settlements.'" *In re Rhone-Poulenc Rorer Inc.*, 51 F.3d 1293, 1298 (7th Cir.) (quoting Henry J. Friendly, *Federal Jurisdiction: A*

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[8] In 2008, 210 federal securities class actions were filed—a 19% increase over the number of 2007 filings and 9% increase over the previous ten-year average. Cornerstone Research, *Securities Class Action Filings, 2008: A Year in Review* 2 (2009), *available at* http://securities.stanford.edu/clearinghouse_research/2008_YIR/20090106_YIR08_Full_Report.pdf. Even more class actions may be sparked by the financial crisis of 2008.

General View 120 (1973)), *cert. denied*, 516 U.S. 867 (1995). In the 36 years since Judge Friendly made that observation, the problem of "blackmail settlements" in federal class actions has only grown as courts, like the Seventh Circuit below, have misapplied and eroded Rule 23's requirements.

The empirical evidence underscores that, despite the importance of certification, courts are not subjecting certification motions to the "'rigorous analysis'" demanded by Rule 23. *Hydrogen Peroxide*, 552 F.3d at 309 (quoting *Gen. Tel. Co.*, 457 U.S. at 161). For example, one recent Federal Judicial Center empirical study examined the certification decisions of four representative district courts over a two-year period and found that Rule 23(b)(3) classes were "certified in 94% to 100% of the securities cases," even though "[i]n all or nearly all" of such cases defendants opposed certification, often because of conflicts of interests. Thomas E. Willging et al., *An Empirical Analysis of Rule 23 To Address the Rulemaking Challenges*, 71 N.Y.U. L. Rev. 74, 89-90 (1996).

The Seventh Circuit's decision in this case further degrades Rule 23's requirements and invites ever-more adventurous class action litigation. Indeed, class action plaintiffs are already pointing to the decision below to argue that injury is irrelevant to the Rule 23 inquiry, *see, e.g.*, *Reed v. Advocate Health Care*, No. 06-C-3337, 2009 WL 3146999, at *6 n.7 (N.D. Ill. Sept. 28, 2009); *Kreger v. General Steel Corp.*, Memorandum in Support of Motion To Certify the Class, 2009 WL 2492895 (E.D. La. July 27, 2009) (No. 07-575), and to argue that courts should shift to the defendants the burden to prove that a class is overbroad, Christopher L. Lebsock, *PIMCO: Another Guidepost for Class*

Certification, Law 360 (Sept. 23, 2009), *at* http://competition.law360.com/articles/123912.

It has been nearly a decade since this Court has comprehensively addressed Rule 23. *See Ortiz*, 527 U.S. 815; *Amchem*, 521 U.S. 591. And as courts and commentators have recognized, the Court has yet to resolve critical issues concerning the certification determination. *See, e.g.*, *Hydrogen Peroxide*, 552 F.3d at 316 ("The Supreme Court has described the [Rule 23] inquiry as a 'rigorous analysis,' and 'close look,' but it has elaborated no further.") (citations omitted); Alfred J. Lechner, Jr. & Helena A. Lynch, *New Defense Strategies for Class Certification Hearings*, 6 Sec. Litig. Rep. 1 (2009) ("[T]he [Supreme] Court has not addressed the precise standard of proof for class certification."); *Class Certification in the Age of Aggregate Proof*, 84 N.Y.U. L. Rev. at 99 ("With so much riding on the class certification determination, one would think that procedural law would have arrived quickly at a clear and broadly shared understanding of the nature of that determination and the permissible parameters for inquiry by the court. That, however, has not been so."). In the absence of such guidance, the lower courts have divided on critical questions concerning the class certification inquiry.

This case provides an ideal vehicle for the Court to provide overdue guidance in this important area of law.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

Josef A. KOHEN, et al., on their own behalf and that of all others similarly situated, Plaintiffs-Appellees,

v.

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC and PIMCO Funds, Defendants-Appellants.

No. 08-1075.

Argued April 1, 2009.
Decided July 7, 2009.

Rehearing and Rehearing En Banc*
Denied July 31, 2009.

571 F.3d 672

Before POSNER, EVANS, and TINDER, Circuit Judges.

POSNER, Circuit Judge.

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* Circuit Judge Ilana Diamond Rovner did not participate in the consideration of this petition for rehearing.

The defendants in this class action suit have appealed from the district court's certification of a plaintiff class. Fed.R.Civ.P. 23(f). The suit, based on section 22(a) of the Commodity Exchange Act, 7 U.S.C. § 25(a), accuses the defendants, collectively "PIMCO," of having violated section 9(a) of the Act, 7 U.S.C. § 13(a), by cornering a futures market. A corner is a form of monopolization. See *United States v. Patten*, 226 U.S. 525, 539-42, 33 S.Ct. 141, 57 L.Ed. 333 (1913); *Great Western Food Distributors, Inc. v. Brannan*, 201 F.2d 476, 478-79 (7th Cir.1953); *Peto v. Howell*, 101 F.2d 353, 358-59 (7th Cir.1939); Robert W. Kolb & James A. Overdahl, *Understanding Futures Markets* 80 (6th ed.2006) ("a successful effort by a trader or group of traders to influence the price of a futures contract by intentionally acquiring market power in the deliverable supply of the underlying good while simultaneously acquiring a large long futures position").

The class consists of persons who between May 9 and June 30, 2005, bought a futures contract on the Chicago Board of Trade in 10-year U.S. Treasury notes. Earlier they had sold such notes short, and the purchases they made between May 9 and June 30 were pursuant to contracts they had with other investors, including PIMCO, to deliver to a commodity clearinghouse, for those investors' accounts, on June 30, a specified quantity of the notes at the price specified in the futures contracts. With rare exceptions, however, futures speculations are completed not by delivery of the underlying commodity (such as milk, or pork bellies, or in this case Treasury notes) to the clearinghouse, though that is an option, but by the making of offsetting futures contracts, as described in Kolb & Overdahl, *supra*, at 17; Mark J.

Powers & Mark G. Castelino, *Inside the Financial Futures Markets* 20 (3d ed.1991); Jeffrey Williams, *The Economic Function of Futures Markets* 9-10 (1989); James M. Falvey & Andrew N. Kleit, "Commodity Exchanges and Antitrust," 4 *Berkeley Bus. L.J.* 123, 127-28 (2007); see also C.B. Reehl, *The Mathematics of Options Trading* 15 (2005). The following table illustrates the process.

Futures Contracting

Day	*Price*	*Trade*	*SS's position*	*B's position*
1	$1,000	*SS* sells contract (to deliver pork bellies) to *B*.	*SS* deposits $100 (10% of the value of the contract) in his account with clearinghouse (required margin); acquires the obligation to deliver pork bellies to clearinghouse.	*B* deposits $100 in his account; acquires the right to require delivery of pork bellies from clearinghouse.
2	$1,500	None	*SS*'s account falls to-$400, so *SS* must deposit $500 in his account to maintain his 10% margin; *SS* is still obligated to deliver pork bellies to the clearinghouse.	*B*'s account increases to $600; *B* still has the right to require delivery of pork bellies from the clearinghouse.
3	$1,500	*SS* caps his losses and buys contract (to deliver pork bellies) from *B*.	*SS*'s trade extinguishes his original contract: his obligation to deliver to the clearinghouse is offset by his right to require delivery from the clearinghouse.	*B*'s trade extinguishes his original contract: his right to require delivery from the clearinghouse is offset by his obligation to deliver to the clearinghouse.

In the example in the table, a short seller, *SS*, sells a specified quantity of pork bellies to *B* (buyer) at a price of $1,000 for delivery in June (hence a "June Contract"). *SS* hopes the price will fall by then. But before the delivery date arrives the price rises to $1,500, and *SS* decides to cap his losses. The simplest way to do this, as in the table, is for *SS* to buy from *B* the same quantity of pork bellies as *SS* had sold to *B*, paying $1,500. *SS* now has offsetting contracts to sell and to buy the same number of pork bellies, and *B* now has offsetting contracts to buy and sell the same number of pork bellies, so neither has a delivery obligation. Neither *wants* to have such an obligation, because both are speculators rather than farmers or meat packers. (Notice in the table that losses and gains are debited and credited to the traders' accounts with the clearinghouse every day, to minimize the risk of loss to the clearinghouse, which guarantees the fulfillment of the futures contract. But this detail plays no role in this case.)

Changes in the demand for or the supply of the underlying commodity will make the price of a futures contract change over the period in which the contract is in force. If the price rises, the "long" (the buyer) benefits, as in our example, and if it falls the "short" (the seller) benefits. But a buyer may be able to force up the price by "cornering" the market—in this case by buying so many June contracts for 10-year Treasury notes that sellers can fulfill their contractual obligations only by dealing with that buyer. *United States v. Patten*, *supra*, 226 U.S. at 539-41, 33 S.Ct. 141; *Zimmerman v. Chicago Board of Trade*, 360 F.3d 612, 616 (7th Cir.2004); *Board of Trade v. SEC*, 187 F.3d 713, 724 (7th Cir.1999) ("a person who owns a substantial portion of the long interest near the

contract's expiration date also obtains control over the supply that the shorts need to meet their obligations. Then the long demands delivery, and the price of the commodity skyrockets. It takes time and money to bring additional supplies to the delivery point, and the long can exploit these costs to force the shorts to pay through the nose"); Roberta Romano, "A Thumbnail Sketch of Derivative Securities and Their Regulation," *55 Md. L.Rev.* 1, 29-30 (1996); "United States Commodity Futures Trading Com-mission Glossary," www. cftc.gov/educationcenter/glossary/glossary_co. html (visited June 10, 2009).

Board of Trade v. SEC, *supra*, 187 F.3d at 725, remarks that since the possibility of manipulation "comes from the potential imbalance between the deliverable supply and investors' contract rights near the expiration date[,] ... [f]inancial futures contracts, which are settled in cash, have no 'deliverable supply'; there can never be a mismatch between demand and supply near the expiration, or at any other time." But while it is correct that most financial futures contracts are settled in cash, *CFTC v. Zelener*, 373 F.3d 861, 865 (7th Cir.2004); Kolb, *supra*, at 16, and that if a cash option exists there is no market to corner (no one can corner the U.S. money supply!), futures contracts traded on the Chicago Board of Trade for ten-year U.S. Treasury notes are an exception; they are not "cash settled." Short sellers who make delivery must do so with approved U.S. Treasury notes; otherwise they must execute offsetting futures contracts. Chicago Board of Trade Rulebook, "Chapter 19: Long-Term U.S. Treasury Note Futures (6½ to 10-Year)," www.cmegroup.com/rulebook/CBOT/V/19/19.pdf (visited June 22, 2009); CME Group, "U.S. Treasury Futures Delivery Process," (4th ed.2008),

w ww.cmegroup.com/trading/interest-rates/files/CL-100_TFDPBrochure-FINAL.pdf (visited June 22, 2009).

The note approved for delivery in this case was the "2/12 Treasury Note" (a Treasury note that expires in February 2012). The plaintiffs claim that PIMCO increased the percentage of these notes that it owned from 12 to 42 percent over a two-week span, with the result that they would have had to pay a monopoly price to get enough notes to close out their contracts. So instead they made offsetting futures contracts, and they claim that as a result they lost more than $600 million, the amount they would have saved had they been able to buy offsetting contracts at a competitive price. (These are just allegations; we do not vouch for their correctness.)

The class certified by the district court consists, as we said, of all persons who between May 9 and June 30, 2005, bought a June Contract in order to close out a short position. PIMCO challenges the definition on the ground that it includes persons who lack "standing" to sue because they did not lose money in their speculation on the June Contract. For example, some of the class members might have taken both short and long positions (in order to hedge—that is, to limit their potential losses) and made more money in the long positions by virtue of PIMCO's alleged cornering of the market than they lost in their short positions. The plaintiffs acknowledge this possibility but argue that its significance is best determined at the damages stage of the litigation. If PIMCO is found to have cornered the market in the June Contract, then each member of the class will have to submit a claim for the damages it sustained as a result of the corner. *Carnegie v. Household Int'l*, 376 F.3d 656, 661 (7th

Cir.2004); 7AA Charles Alan Wright, Arthur R. Miller & Mary Kay Kane, *Federal Practice & Procedure* § 1784 (2009). Some of the class members, discovering that they were not injured at all, will not submit a claim, and others will submit a claim that will be rejected because the claimant cannot prove damages, having obtained off-setting profits from going long.

PIMCO argues that before certifying a class the district judge was required to determine which class members had suffered damages. But putting the cart before the horse in that way would vitiate the economies of class action procedure; in effect the trial would precede the certification. It is true that injury is a prerequisite to standing. But as long as one member of a certified class has a plausible claim to have suffered damages, the requirement of standing is satisfied. *United States Parole Commission v. Geraghty*, 445 U.S. 388, 404, 100 S.Ct. 1202, 63 L.Ed.2d 479 (1980); *Wiesmueller v. Kosobucki*, 513 F.3d 784, 785-86 (7th Cir.2008). This is true even if the named plaintiff (the class representative) lacks standing, provided that he can be replaced by a class member who has standing. "The named plaintiff who no longer has a stake may not be a suitable class representative, but that is not a matter of jurisdiction and would not disqualify him from continuing as class representative until a more suitable member of the class was found to replace him." *Id.* at 786.

Before a class is certified, it is true, the named plaintiff must have standing, because at that stage no one else has a legally protected interest in maintaining the suit. *Id.*; *Sosna v. Iowa*, 419 U.S. 393, 402, 95 S.Ct. 553, 42 L.Ed.2d 532 (1975); *Walters v. Edgar*, 163 F.3d 430, 432-33 (7th Cir.1998); *Murray v. Auslander*, 244 F.3d 807, 810 (11th Cir.2001). And while ordinarily an

unchallenged allegation of standing suffices, a colorable challenge requires the plaintiff to meet it rather than stand mute. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 561, 112 S.Ct. 2130, 119 L.Ed.2d 351 (1992). PIMCO tried to show in the district court that two of the named plaintiffs could not have been injured by the alleged corner. We need not decide whether it succeeded in doing so, because even if it did, that left one named plaintiff with standing, and one is all that is necessary.

If the case goes to trial, this plaintiff may fail to prove injury. But when a plaintiff loses a case because he cannot prove injury the suit is not dismissed for lack of jurisdiction. Jurisdiction established at the pleading stage by a claim of injury that is not successfully challenged at that stage is not lost when at trial the plaintiff fails to substantiate the allegation of injury; instead the suit is dismissed on the merits. *American Civil Liberties Union v. St. Charles*, 794 F.2d 265, 269 (7th Cir.1986). Pressed at argument, PIMCO's counsel retreated, conceded or at least seemed to concede that the issue was not jurisdictional, and clarified that his argument was only that the class members lacked "statutory standing." Then he took back his concession, arguing that if any class member were found not to have sustained damages, the court would have no jurisdiction over that class member, who would therefore not be bound by any judgment or settlement and so could bring his own suit for damages. That is to say that if a plaintiff loses his case, this shows that he had no standing to sue and therefore can start over. That would be an absurd result, and PIMCO need not fear it. *Id.*; *Bruggeman v. Blagojevich*, 324 F.3d 906, 909 (7th Cir.2003).

The term "statutory standing" is found in many cases, e.g., *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 830, 119 S.Ct. 2295, 144 L.Ed.2d 715 (1999); *Steel Co. v. Citizens for a Better Environment*, 523 U.S. 83, 96-97 and n. 2, 118 S.Ct. 1003, 140 L.Ed.2d 210 (1998); *United States v. U.S. Currency, in Amount of $103,387.27*, 863 F.2d 555, 560-61 and n. 10 (7th Cir.1988), but it is a confusing usage. It usually refers to a situation in which, although the plaintiff has been injured and would benefit from a favorable judgment and so has standing in the Article III sense, he is suing under a statute that was not intended to give him a right to sue; he is not within the class intended to be protected by it. *Steel Co. v. Citizens for a Better Environment, supra*, 523 U.S. at 97, 118 S.Ct. 1003; *Warth v. Seldin*, 422 U.S. 490, 500, 95 S.Ct. 2197, 45 L.Ed.2d 343 (1975); *Harzewski v. Guidant Corp.*, 489 F.3d 799, 803-04 (7th Cir.2007). This is not such a case.

What is true is that a class will often include persons who have not been injured by the defendant's conduct; indeed this is almost inevitable because at the outset of the case many of the members of the class may be unknown, or if they are known still the facts bearing on their claims may be unknown. Such a possibility or indeed inevitability does not preclude class certification, *Carnegie v. Household Int'l, supra*, 376 F.3d at 661; 1 Alba Conte & Herbert Newberg, *Newberg on Class Actions* § 2:4, pp. 73-75 (4th ed.2002), despite statements in some cases that it must be reasonably clear at the outset that all class members were injured by the defendant's conduct. *Adashunas v. Negley*, 626 F.2d 600, 604 (7th Cir.1980); *Denney v. Deutsche Bank AG*, 443 F.3d 253, 264 (2d Cir.2006). Those cases focus on the class definition; if the definition is so broad that it sweeps within it persons

who could not have been injured by the defendant's conduct, it is too broad.

A related point is that a class should not be certified if it is apparent that it contains a great many persons who have suffered no injury at the hands of the defendant, see *Oshana v. Coca-Cola Co.*, 472 F.3d 506, 514-15 (7th Cir.2006); *Romberio v. Unumprovident Corp.*, 2009 WL 87510, at *8 (6th Cir. Jan.12, 2009); cf. *Brown v. American Honda*, 522 F.3d 6, 28-29 (1st Cir.2008), if only because of the *in terrorem* character of a class action. *In re Bridgestone/Firestone Tires Products Liability Litigation*, 288 F.3d 1012, 1015-16 (7th Cir.2002); *Parker v. Time Warner Entertainment Co., L.P.*, 331 F.3d 13, 22 (2d Cir.2003); *EP Medsystems, Inc. v. EchoCath, Inc.*, 235 F.3d 865, 881 (3d Cir.2000). When the potential liability created by a lawsuit is very great, even though the probability that the plaintiff will succeed in establishing liability is slight, the defendant will be under pressure to settle rather than to bet the company, even if the betting odds are good, *Blair v. Equifax Check Services*, 181 F.3d 832, 834 (7th Cir.1999); *In re Rhone-Poulenc Rorer Inc.*, 51 F.3d 1293, 1297-1300 (7th Cir.1995). For by aggregating a large number of claims, a class action can impose a huge contingent liability on a defendant. PIMCO is a very large firm, however, with assets under management of more than $750 billion, www.pimco.com/LeftNav/PressCenter/PIMCOFacts.htm (visited June 10, 2009). This suit does not jeopardize its existence. But it has good reason not to want to be hit with a multi-hundred-million-dollar claim that will embroil it in protracted and costly litigation—the class has more than a thousand members, and determining the value of their

claims, were liability established, might thus require more than a thousand separate hearings.

So if the class definition clearly were overbroad, this would be a compelling reason to require that it be narrowed. *Adashunas v. Negley*, *supra*, 626 F.2d at 603-04; *Robidoux v. Celani*, 987 F.2d 931, 937 (2d Cir.1993); *Eastland v. Tennessee Valley Authority*, 704 F.2d 613, 617-18 (11th Cir.1983); 7AA Charles Alan Wright *et al.*, *supra*, § 1760, pp. 139-49; cf. *Crawford v. Equifax Payment Services*, 201 F.3d 877, 882 (7th Cir.2000). But this has not yet been shown. Although some of the class members probably were net gainers from the alleged manipulation, there is no reason at this stage to believe that many were. A short seller hopes the price of the security that he's selling will fall. He knows it may rise and his speculative gamble therefore fail, but if the rise is caused or increased by a violation of law the incremental loss caused by the violation entitles him to an award of damages. And while it is true that short sellers may want to hedge part of the risk of a rise in the price of the security that they are selling short, they will not hedge the *entire* risk, as that would eliminate the prospect of speculative gains that motivates short selling. Suppose a short seller sells a security at $80, hoping the price will fall below that by the delivery date; but fearing that it might rise far enough to bankrupt him, he hedges by contracting to buy the security at $100 should it rise that high. That will cap his potential loss at $20, but he will sustain a loss if the defendant drives the price of the security to any level above $80.

A further possibility, however, is that some of the members of the class were actually speculating on a rise in the price of the June Contract, and made some short sales merely as a hedge, and because of PIMCO's

alleged conduct obtained a net profit. We do not know how many of these "long" speculators the class may contain, but probably not many. Otherwise PIMCO would not have made huge purchases of the June Contract in order to drive up the price at which short sellers would have to close out their sales. Put differently, were there not a great many net short sellers of the June Contract, PIMCO could not have driven its price to an artificially high level because only short sellers would buy at such a price, for they alone would have to close out their short positions by buying the June Contract. (Not that the plaintiffs have *proved* that PIMCO tried to corner the market, or succeeded; but at this stage in the proceeding we must assume that they can prove it.)

So while PIMCO states correctly in its reply brief that "a proper class definition cannot be so untethered from the elements of the underlying cause of action that it wildly overstates the number of parties that could possibly demonstrate injury," it has failed to justify the use of the word "wildly" to describe the extent to which the class definition may be too broad.

PIMCO's repeated, indeed obsessive, citations to the Supreme Court's decision in *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336, 125 S.Ct. 1627, 161 L.Ed.2d 577 (2005), a case that does not involve class certification, suggests desperation. The Court held in that case that an allegation that the plaintiffs had bought securities at "artificially inflated prices" did not state a claim that the plaintiffs had been injured by the inflation because, for all that appeared, the prices had remained at that level, or even a higher one, or the plaintiffs had sold before the price bubble burst. The Court refused to "allow recovery where a misrepresentation leads to an inflated purchase price

but nonetheless does not proximately cause any economic loss." *Id.* at 346, 125 S.Ct. 1627. In this case, too, the plaintiffs claim that the defendants forced up the price, but there the resemblance between the two cases ends. The plaintiffs sold short, so, prima facie at least—being forced as they were to cover by June 30—they were injured if the price of cover was artificially inflated during the period between their sale and the delivery date.

At argument PIMCO's lawyer told us that he could obtain names of class members. If so, he can, as in *Bell v. Farmers Ins. Exchange*, 115 Cal.App.4th 715, 9 Cal.Rptr.3d 544, 550-51, 568, 571 (2004), and *Long v. Trans World Airlines, Inc.*, 1988 WL 87051, at *1 (N.D.Ill. Aug.18, 1988), depose a random sample of class members to determine how many were net gainers from the alleged manipulation and therefore were not injured, and if it turns out to be a high percentage he could urge the district court to revisit its decision to certify the class. Cf. *Hilao v. Estate of Marcos*, 103 F.3d 767, 782-84 (9th Cir.1996); *Long v. Trans World Airlines, Inc.*, 761 F.Supp. 1320, 1325-30 (N.D.Ill.1991); *Marisol A. v. Giuliani*, 1997 WL 630183, at *1 (S.D.N.Y. Oct.10, 1997). PIMCO has not done this; should it take the hint and try to do so now, this will be an issue for consideration by the district judge.

PIMCO also argues that class certification should have been denied because of potential conflicts of interest among class members that will make it impossible for class counsel to represent all of them all impartially. Fed.R.Civ.P. 23(a)(4); *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 625-26, 117 S.Ct. 2231, 138 L.Ed.2d 689 (1997); *Secretary of Labor v. Fitzsimmons*, 805 F.2d 682, 697 (7th Cir.1986); *Valley Drug Co. v. Geneva Pharmaceuticals, Inc.*, 350 F.3d

1181, 1189 (11th Cir.2003); *Pickett v. Iowa Beef Processors*, 209 F.3d 1276, 1280-81 (11th Cir.2000). Class members covered by buying the June Contract, thus capping their losses, at different times during the seven-week period embraced by the complaint. One who covered very early would want to show that the effect of PIMCO's alleged misconduct peaked then. Moreover, the curve of rising prices for the June Contract dipped at one point during the complaint period and class members who covered during the dip might want to show that PIMCO's effect on the price level was completed by then and the post-dip rise in prices was due to market forces for which PIMCO was not responsible. Suppose the price had risen from $100 at the beginning of the complaint period to $130 at the bottom of the dip, and from $130 to $150 between then and the delivery date. Short sellers who covered during the dip would want to show that it was PIMCO who pushed the price up from $100 to $130, and that insofar as market forces were shown to be responsible for part of the price rise they operated after the dip rather than before. Short sellers who covered at the end of the period would want to show that the entire price increase, from $100 to $150, was due to PIMCO's illegal activity.

At this stage in the litigation, the existence of such conflicts is hypothetical. If and when they become real, the district court can certify subclasses with separate representation of each, Fed.R.Civ.P. 23(c)(5); *Reynolds v. Beneficial Nat'l Bank*, 288 F.3d 277, 282 (7th Cir.2002); *Blackie v. Barrack*, 524 F.2d 891, 909 (9th Cir.1975); 7AA Charles Alan Wright *et al.*, *supra*, § 1769.1, pp. 455-58, if that would be consistent with manageability. *In re Cendant Corp. Securities Litigation*, 404 F.3d 173, 201 (3d Cir.2005); John C.

Coffee Jr., "Class Action Accountability: Reconciling Exit, Voice, and Loyalty in Representative Litigation," 100 *Colum. L.Rev.* 370, 398 (2000). To deny class certification now, because of a potential conflict of interest that may not become actual, would be premature. *Int'l Woodworkers of America, etc. v. Chesapeake Bay Plywood Corp.*, 659 F.2d 1259, 1269 (4th Cir.1981); 1 Conte & Newberg, *supra*, § 3.25, p. 422; cf. *Smilow v. Southwestern Bell Mobile Systems, Inc.*, 323 F.3d 32, 40 (1st Cir.2003).

PIMCO's attempt to derail this suit at the outset is ill timed, ill conceived, and must fail. The district court's class certification is

AFFIRMED.

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
Eastern Division

Josef A. KOHEN, Breakwater Trading LLC, and Richard Hershey, Plaintiffs,

v.

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC, PIMCO Funds, and John Does 1-100, Defendants.

No. 05 C 4681

July 31, 2007

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244 F.R.D. 469

MEMORANDUM OPINION AND ORDER

RONALD A. GUZMÁN, District Judge.

Plaintiffs Breakwater Trading LLC ("Breakwater") and Richard Hershey have filed this class action against Pacific Investment Management LLC ("PIMCO") and PIMCO Funds alleging violations of §§ 9(a), 22(a) and 22(a)(1) of the Commodity Exchange Act ("CEA"). 7 U.S.C. §§ 13(a), 25(a), 25(a)(1). Plaintiffs now move for class certification pursuant to Federal Rule of Civil Procedure ("Rule") 23. Additionally, defendants have moved to dismiss the

complaint for failure to state a claim pursuant to Rule 12(b)(6). For the reasons set forth in this opinion, the Court grants plaintiffs' motion for class certification, denies PIMCO Funds' motion to dismiss, and grants in part and denies in part PIMCO's motion to dismiss,

Facts

This is a class action brought by plaintiffs on behalf of purchasers of the June 2005 Ten-Year Treasury note futures contract ("June Contract"). (Pls.' Mem. Supp. First Am. Mot. Class Cert. ("Pls.' Mem. Supp. Mot. Class Cert.") 1.) Plaintiffs allege defendants manipulated and aided and abetted the manipulation of prices of the June Contract and the cheapest-to-deliver ("CTD") Treasury note underlying the June Contract in violation of §§ 9(a), 22(a) and 22(a)(1) of the CEA. (*Id.*)

Futures contracts are standardized according to terms specified by the commodities exchange that creates the contract, which mattes such contracts fungible and allows them to be bought and sold over the exchange. (Compl. ¶ 29; PIMCO's Mem. Supp. Mot. Dismiss 3.) The party contracting to sell the underlying commodity pursuant to a futures contract is called the "short," and is said to have a "short position." (PlMCO's Mem. Supp, Mot. Dismiss 3-4.) The party contracting to buy the underlying commodity pursuant to a futures contract is called the "long," and is said to have a "long position." (*Id.*) The long position has the right to take delivery of the underlying commodity, while the short position is obligated to make delivery to the long position. (*Id.*) A party to a futures contract can "liquidate" its position by entering into an equal and opposite transaction (*i.e.*, "offset") in the futures market prior to the expiration of trading on the futures contract. (*Id.* at 4.)

Plaintiffs Hershey and Breakwater purchased June Contracts during the class period to liquidate a short position and incurred a loss on the transaction. (Compl.¶¶ 18-19.) PIMCO is an institutional money manager, and PIMCO Funds is a Massachusetts trust and registered open-end management investment company consisting of separate portfolios. (*Id.* ¶¶ 22-23.) PIMCO Funds does not make any investment decisions or execute trades; rather, PIMCO Funds contracts with its investment advisor, PIMCO, (PIMCO Funds' Mem. Supp. Mot. Dismiss 2.) Plaintiffs refer to PIMCO and PIMCO Funds collectively in their complaint, (Compl.¶ 23.) Plaintiffs allege that between the years 2000 to 2004 the volume and open interest of the Chicago Board of Trade ("CBT") Ten-Year Treasury note futures contract steadily increased while the available supply of Treasury notes deliverable in satisfaction of the futures contracts remained constant or declined, which made the futures contract susceptible to manipulation by a person in control of a large long position. (Pls.' Mem. Supp. Mot. Class Cert. 3.) In late 2004 and 2005, and with knowledge of the foregoing facts, defendants began to accumulate a large long position in the June Contract. (Compl.¶¶ 2, 45.) By March 31, 2005, defendants held in excess of $16.3 billion in the June Contract, which plaintiffs claim is of unprecedented size and was many times larger than defendants' position prior to October 2004. (*Id.* ¶ 53; Pls.' Mem. Supp. Mot, Class Cert, 3.) This long position exceeded the available supply of the CTD Treasury note. (Pls.' Mem. Opp'n PIMCO's Mot. Dismiss 6.)

Additionally, from March 20, 2005 until the end of June 2005, defendants increased their holdings of the February 2012 Treasury note (the "CTD Treasury note") to $13.3 billion, which was the CTD Treasury

note for the June Contract and was in excess of 75% of the deliverable supply of such notes. (Compl, ¶¶ 5, 34, 37, 56, 58; Pls.' Mem. Supp. Mot. Class Cert. 4.) However, defendants argue that the $13.3 billion amounted to merely 3.16% of the notes deliverable under the terms of the June Contract. (PIMCO's Mem. Supp. Mot, Dismiss 6.)

The CBT rules specify a number of different Treasury note issues with maturity dates ranging from six-and-one-half to ten years that are acceptable for delivery against a Ten-Year Treasury note futures contract. (Compl.¶ 33.) Although multiple Treasury note issues are typically deliverable against a particular futures contract, usually a single Treasury note is most economical for shorts to deliver, which is referred to as the CTD. (*Id.* ¶ 34.)

As the June Contract neared its expiration, and coinciding with a decline in the open interest of the June Contract in May and June 2005, defendants held their long position in the June Contract, which plaintiffs claim is "highly unusual." (*Id.* ¶ 4; Pls.' Mem. Supp. Mot. Class Cert. 4; Pls.' Mem. Opp'n PIMCO's Mot. Dismiss 6.) After trading in the June Contract closed, defendants represented that they took deliveries on the June Contract (which, according to plaintiffs, occurs less than 1% of the time because traders usually offset their future contract positions before their contracts mature) and acquired a large position in the CTD Treasury note for investment purposes. (Compl. ¶ 30; Pls.' Mem. Supp. Mot. Class Cert. 4.) However, by September 30, 2005, defendants had sold all of their CTD Treasury note holdings. (Pls.' Mem. Supp. Mot. Class Cert. 4.) On June 29, 2005, the CBT amended CBT Regulation 425.01 to limit the amount of contracts that could be held during the last

ten trading days to 50,000 contracts, which was less than one-third of defendants alleged long position in the June Contract. (Compl. ¶¶ 81-82.)

Plaintiffs allege the motive and intent underlying defendants' conduct was to increase financial returns and profit from artificially high prices. (*Id.* ¶ 92; Pls.' Mem. Opp'n PIMCO's Mot. Dismiss 7.) Throughout the class period, May 9, 2005 to June 30, 2005, the pricing relationships and trading behavior of the June Contract and/or the CTD Note exhibited anomalies, which plaintiffs alleged evinced an artificial market. (Compl. ¶ 62-73; Pls.' Mem. Supp. Mot, Class Cert. 4.)

Discussion

Plaintiffs have moved for class certification pursuant to Rule 23. Additionally, defendants have moved to dismiss the complaint pursuant to Rule 12(b)(6) for failure to state a claim upon which relief can be granted.

I. Motion for Class Certification

Before discussing the merits of plaintiffs' motion for class certification, two preliminary arguments that have been raised by defendants will be considered. Defendants argue that plaintiffs lack standing to bring their individual actions, and that the class definition is fatally flawed because it includes persons that have not been injured by defendants alleged manipulation of the June Contract.

First, defendants argue that neither Hershey nor Breakwater can serve as a representative of the putative class because both plaintiffs lack standing. If the named plaintiffs cannot establish standing, then they may not seek relief on their own behalf or on the behalf of any other members of the class. *O'Shea v. Littleton*, 414 U.S. 488, 494, 94 S.Ct. 669, 38 L.Ed.2d

674 (1974). Defendants assert that § 22 of the CEA imposes the standing requirement that plaintiffs must have purchased or sold a futures contract and suffered actual damages as a result of the price manipulation of the futures contract. 7 U.S.C. § 25(a)(1)(D).

Defendants argue that plaintiffs were not the actual purchasers of the June Contract. According to defendants, plaintiffs entered into a partnership or joint account arrangement, which was the actual purchaser of the contracts. Defendants assert that Breakwater was not even the legal owner of the accounts in which its employees traded, and Hershey held only a minority interest in his joint account. According to defendants, that plaintiffs lack standing is consistent with general principles of jointly held claims. In support of their argument, defendants rely solely on *Shelley v. Noffsinger*, a case in which the court ordered joinder of a party with an interest in the disputed joint account because it was necessary to avoid needless risk of multiple lawsuits, 91 F.R.D. 263, 266-67 (N.D.Ill.1981).

The Court is not persuaded by defendants' argument. In *Hochschuler v. G.D. Searle & Co.*, the defendants argued that the absence of a joint owner rendered the class' named representative's claim atypical, 82 F.R.D. 339, 346 (N.D.Ill.1978). In concluding the claim was not atypical, the court stated that both an individual purchaser and a purchaser that decided to purchase as a co-owner "would be influenced by the same material nondisclosures." *Id.* Similarly, in this case, the same alleged course of conduct by defendants that resulted in manipulation of the price of the June Contract would influence and harm both the individual purchaser and the co-owner of a joint account. Hershey's decision to purchase as a co-owner

of a joint account should not affect his ability to seek remedies under the CEA because Hershey has alleged that he suffered actual damages from purchasing the June Contract at a manipulated price. (Compl.¶ 103.) Therefore, the Court finds that Hershey has standing and may seek to represent other members of the putative class.

Additionally, the Court finds that Breakwater has standing to sue under the § 22 of the CEA. Breakwater has alleged that it purchased one or more June Contracts during the class period and was injured as a result of defendants' manipulative conduct. (*Id.*) Because Breakwater has alleged that it suffered injury, Breakwater has standing and may seek to represent other members of the putative class. *See Moose Lodge No. 107 v. Irvis*, 407 U.S. 163, 166, 92 S.Ct. 1965, 32 L.Ed.2d 627 (1972) ("Appellee has standing to seek redress for injuries done to him, but may not seek redress for injuries done to others."); *see also Indemnified Capital Invs., SA v. R.J. O'Brien & Assocs., Inc.*, 12 F.3d 1406, 1408-10 (7th Cir.1993) (finding plaintiff did not have standing to sue based on "customer accounts," as opposed to plaintiff's "house accounts," because customers alone suffered the loss; further noting that plaintiff did not allege that it was injured by losses sustained in customer accounts).

Second, defendants argue that despite plaintiffs' amendment, the amended class definition still includes class members who were not injured by the alleged manipulation of the June Contract. If class members cannot allege some threatened or actual injury resulting from defendants' illegal actions, then a federal court may not assume jurisdiction because there is no actual case or controversy. *O'Shea*, 414 U.S. at 493-94, 94 S.Ct. 669 (quotations omitted); *Adashunas*

v. Negley, 626 F.2d 600, 604 (7th Cir.1980) (stating it was not reasonably clear that the proposed class members have all suffered a constitutional or statutory violation warranting relief in order to support the requirement of an actual case or controversy). Defendants contend that the amendment to the class definition still does not eliminate those members of class who both bought and sold, which in some cases resulted in a net benefit to those who sold at higher prices than they bought.

The amended class definition includes "[a]ll persons who purchased, between May 3, 2005 and June 30, 2005 ('Class Period'), inclusive, a June 10-year Treasury note futures contract in order to liquidate a short position (the 'Class'). Excluded from the Class are defendants and any affiliated or associated party or defendants." (Pls.' Reply Mem. Supp. Class Cert. 4.) Defendants rely on *Dura Pharmaceuticals, Inc. v. Broudo* in support of the proposition that both sides of transactions by class members who bought and sold within the class period would need to be analyzed and netted to determine whether there was actual injury, 544 U.S. 336, 125 S.Ct. 1627, 161 L.Ed.2d 577 (2005). In *Dura*, the Supreme Court reversed the Ninth Circuit's standard for pleading the element of loss causation for a securities fraud claim. *Id.* at 346, 125 S.Ct. 1627. The Court stated that merely alleging an inflated purchase price is inconsistent with the law's requirement that a plaintiff prove a defendant's fraudulent conduct caused the plaintiff's economic loss. *Id.* However, this is not a securities fraud case and, thus, the elements of proof are different. *Compare id.* at 341-42, 125 S.Ct. 1627 (listing the essential elements of a securities fraud claim: a material misrepresentation, scienter, a connection with the purchase or sale of a security,

reliance, economic loss, and loss causation), *with In re Soybean Futures Litig.*, 892 F.Supp. 1025, 1045 (N.D.Ill.1995) (listing the elements of a price manipulation claim: "(1) the defendant possessed the ability to influence prices; (2) an artificial price existed; (3) the defendant caused the artificial price; and (4) the defendant specifically intended to cause the artificial price."). Therefore, the Court does not find *Dura* controlling on the issue of whether the class definition includes uninjured members. Plaintiffs respond by arguing that all class members allegedly suffered the injury of paying an artificially inflated price for the June Contract. Even with regard to class members that purchased and sold before and during the class period, plaintiffs contend that market manipulation cases have repeatedly certified classes despite issues of net damages for in-and-out traders. *See, e.g., In re Sumitomo Copper Litig.*, 182 F.R.D. 85, 92 (S.D.N.Y.1998) (stating, in regard to in-and-out traders, that "factual differences in the amount of damages, date, ... the presence of both purchasers and sellers, and other such concerns will not defeat class action certification when plaintiffs allege that the same unlawful course of conduct affected all members of the proposed class.").

The Court finds that the amended class definition does not suffer from a fatal flaw. At this stage of the litigation, it would be premature to deny plaintiffs the opportunity to unify in their task to prove that defendants engaged in a common course of conduct that negatively affected all members of the proposed class. Plaintiffs allege that defendants' conduct manipulated the price of the June Contract upward to an artificial level, and, thus, each purchaser of a June Contract within the class period would have paid a

higher price than would otherwise be the case absent the alleged manipulation. Therefore, the Court is satisfied that all members of the class have suffered injury, and defendants' concerns over the final determination of net damages for some individual members of the class should be resolved in the damages stage of the litigation.[1] *See Katz v. Comdisco, Inc.*, 117 F.R.D. 403, 412 (N.D.Ill.1987) ("Traditionally ... the courts have not allowed individual questions of damages to prevent class certification."); *In re LTV Sec. Litig.*, 88 F.R.D. 134, 148 (N.D.Tex.1980) ("[O]ne who has both bought and sold in the 'tainted market' may nonetheless have suffered an injury. Inquiry into matters of the measure of damage is not ordinarily made at the class certification stage."). Because defendants two preliminary arguments are not dispositive, the Court will move on to consider the merits of plaintiffs' motion for class certification.

"[A] district court has broad discretion to determine whether certification of a class is appropriate." *Retired Chi. Police Ass'n v. City of Chi.*, 7 F.3d 584, 596 (7th Cir.1993). The putative class representative has the burden of establishing four prerequisites to class certification: (1) the class is too numerous to join all members, (2) there are common questions of law or fact common to the case, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class. *Id.*; Fed.R.Civ.P. 23(a). Failure to satisfy any of

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[1] Defendants' concerns about the inclusion of class members that did not suffer actual damages will further be considered and analyzed infra in connection with the requirements of Rule 23.

the prerequisites will preclude certification of the class. *Retired Chi. Police Ass'n*, 7 F.3d at 596. "Before deciding whether to allow a case to proceed as a class action ... a judge should make whatever factual and legal inquiries ... necessary under Rule 23" *Szabo v. Bridgeport Machs., Inc.*, 249 F.3d 672, 676 (7th Cir.2001).

A. Rule 23(a) Requirements

1. Numerosity

To satisfy the numerosity requirement, "the class must be so numerous that joinder of all members is impracticable." Fed.R.Civ.P. 23(a)(1). Plaintiffs are not required to specify the number of members with exactness, *Marcial v. Coronet Insurance Co.*, 880 F.2d 954, 957 (7th Cir.1989), and, to support a finding of numerosity, the court is entitled to make common-sense assumptions, *Peterson v. H & R Block Tax Servs.*, 174 F.R.D. 78, 81 (N.D.Ill.1997).

Plaintiffs allege that there are over one thousand class members around the United States whose identities can be ascertained through CBT records. (Compl. ¶ 95; Pls.' First Am. Mot. Class Cert. ¶ 4.) Defendants fail to dispute the numerosity requirement, and the Court is satisfied that the number members in the proposed class is large enough to render joinder impracticable.

2. Commonality

To satisfy the commonality requirement, there must be questions of law or fact common to the class. Fed.R.Civ.P. 23(a)(2). "A common nucleus of operative fact is usually enough to satisfy the commonality requirement," and "[t]he fact that there is some factual variation among the class ... will not defeat a class action." *Rosario v. Livaditis*, 963 F.2d 1013, 1017-18

(7th Cir.1992). The commonality requirement has been referred to as a low hurdle that is easily surmounted. *Gaspar v. Linvatec Corp.*, 167 F.R.D. 51, 57 (N.D.Ill.1996); *In re Prudential Sec. Inc., Ltd. P'ships Litig.*, 163 F.R.D. 200, 206 (S.D.N.Y.1995); *Scholes v. Stone, McGuire & Benjamin*, 143 F.R.D. 181, 185 (N.D.Ill.1992). Commonality is satisfied as long as one question of law or fact is common to the class. *Tylka v. Gerber Prods. Co.*, 178 F.R.D. 493, 496 (N.D.Ill.1998); *Arenson v. Whitehall Convalescent & Nursing Home, Inc.*, 164 F.R.D. 659, 663 (N.D.Ill.1996).

Plaintiffs assert that questions of law are common to all members of the class. Under the CEA, they argue, the same elements for claims of manipulation and for claims of aiding and abetting manipulation are applicable to all class members. Defendants fail to dispute plaintiffs' assertion that common questions of law exist. Furthermore, plaintiffs argue that common questions of fact will arise as they seek to prove historical facts such as ordinary Treasury note futures prices, volumes, open interests, as well as industry practices. Plaintiffs argue that all class members will want to develop this historical information database, which will require extensive discovery and expert testimony, in order to establish whether and to what extent defendants' conduct caused the Treasury note futures prices to become artificial. Plaintiffs have established that there are questions of law and fact common to all members of the putative class.

3. Typicality

The typicality requirement is satisfied if "the claims or defenses of the representative parties are typical of the claims or defenses of the class." Fed. R. Civ, P. 23(a)(3). "A plaintiff's claim is typical if it arises from the same event or practice or course of conduct that

gives rise to the claims of other class members and his or her claims are based on the same legal theory." *De La Fuente v. Stokely-Van Camp, Inc.*, 713 F.2d 225, 232 (7th Cir.1983); *see Rosario*, 963 F.2d at 1018 ("[W]e look to the defendant's conduct and the plaintiff's legal theory to satisfy Rule 23(a)(3)."). Even if there are factual distinctions between the representative parties and other class members, the typicality requirement can be satisfied. *De La Fuente*, 713 F.2d at 232. "Thus, similarity of legal theory may control even in the face of difference of fact." *Id.* Defendants assert that plaintiffs are not typical of the putative class. Defendants note that "[i]f proof of [plaintiffs'] claims would not necessarily prove all of the proposed class members' claims," then the typicality prong is not satisfied. *Williams v. Ford Motor Co.*, 192 F.R.D. 580, 586 (N.D.Ill.2000) (quotation omitted). Because Hershey only purchased a June Contract on May 11, 2005, defendants contend that Hershey will only have to prove manipulation on that specific day, and he has no incentive to prove claims of the class members that purchased on other dates during the class period. Moreover, defendants contend Hershey's trading during the class period was profitable overall, and thus he is not typical of members that may have lost money overall.

Additionally, defendants assert that Breakwater is not typical of the class members. Defendants claim that Breakwater did not trade through the entire class period and Breakwater's claims focus only on certain days within the class period. Specifically, defendants state that market volatility on the dates Breakwater traded resulted from an announcement on May 24, 2005 made by the Federal Reserve Board's Federal Open Market Committee. Thus, defendants contend

Breakwater will have to litigate this issue individually, which renders Breakwater's claim atypical of other members of the class who do not have to address the Federal Reserve Board issue.

Plaintiffs argue that they are typical of members of the class because their claims are predicated on defendants' common course of conduct or scheme to create artificial prices for the June Contract. Plaintiffs contend that in order to prove a price manipulation claim, no class member could merely submit evidence of what occurred on the specific days they traded; rather, to have validity, the class members would need to present historical data.

The Court determines that plaintiffs' claims are typical of members of the class. Defendants are alleged to have engaged in a course of conduct that manipulated prices for the June Contract. All class members purchased the same futures contract within the class period, and, thus, all members were affected by defendants' same course of conduct and alleged price manipulation. Furthermore, all class members seek relief under the CEA based on the same legal theory. Therefore, plaintiffs' claims are typical because they arise from the same events or course of conduct that gives rise to the claims of other class members and are based on the same legal theory. *See De La Fuente*, 713 F.2d at 232.

The fact that plaintiffs did not trade through the entire class period does not preclude class certification. *See In re Sumitomo Copper Litig.*, 182 F.R.D. at 94 ("[T]he simple fact that Class members may have purchased and sold copper futures at different times, for different purposes, does not detract from the fact that every class member purchased or sold the same fungible ... contract in the same centralized ...

market."). Moreover, the Court agrees with plaintiffs that all class members would desire to compile historical evidence, as opposed to merely relying on evidence based on a single date, to support an allegation of price manipulation in order to lend reliability to their claims. Therefore, the fact that plaintiffs traded only on certain dates while members of the class traded on different dates is not dispositive of the typicality issue. *See In re WorldCom, Inc. Sec. Litig.*, 219 F.R.D. 267, 280 (S.D.N.Y.2003) ("[T]he possibility that proof of injury might require separate evaluations of the artificiality of a commodities price at the moments affecting each of the class members need not defeat class certification.").

Even if defendants prove Hershey offset a loss during the class period, Hershey's claim would not be atypical of a class member who sustained a loss. *See Blackie v. Barrack*, 524 F.2d 891, 905 (9th Cir.1975) ("The amount of damages is invariably an individual question and does not defeat class action treatment."); *In re Natural Gas Commodities Litig.*, 231 F.R.D. 171, 179 (S.D.N.Y.2005) (recognizing the possibility that, although the nature of the manipulation was not yet ascertained by plaintiff, a class member who earned substantial profits through trading in natural gas futures could nonetheless have been damaged by the alleged scheme to manipulate prices higher than they otherwise would have been);[2] *In re Sumitomo Copper*

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[2] The standard relied upon by the *In re Natural Gas Commodities* court to determine whether plaintiffs had adequately alleged Rule 23's requirements has since been overruled. *In re Initial Pub. Offering Sec. Litig.*, 471 F.3d 24, 35 n. 5 (2d Cir.2006) (holding that the "some showing" standard is

Litig., 182 F.R.D. at 93 (rejecting the argument that conflicts of interest in establishing the fact and extent of any manipulation will arise between spread and hedge traders and the proposed class). Finally, the Court determines that the market volatility purportedly caused by the Federal Reserve Board's announcement on May 24, 2005 is not a defense that renders Breakwater's claim atypical of the putative class, A named plaintiff is not a proper class representative only "where it is predictable that a major focus of the litigation will be on an arguable defense that is unique to the named plaintiff." *In re VMS Securities Litig.*, 136 F.R.D. 466, 475 (N.D.Ill.1991). Even if defendants prove that the Federal Reserve Board's announcement affected market prices of the June Contract during the class period and that issue becomes a major focus of the litigation, many members of the class may have an interest in opposing this issue since it occurred in the middle of the class period. For these reasons, the Court determines that plaintiffs have satisfied the typicality requirement.

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overruled, to be replaced with the standard that a judge should resolve any factual disputes relevant to establishing Rule 23 requirements prior to certifying a class). Other class actions certified in the Second Circuit prior to the ruling in *In re Initial Public Offering Securities Litigation* may have also relied on the more lenient standard. *See, e.g., In re Sumitomo Copper Litig.*, 194 F.R.D. 480 (S.D.N.Y.2000); *In re Sumitomo Copper Litig.*, 182 F.R.D. 85 (S.D.N.Y.1998). However, district courts have broad discretion in determining whether to certify a class, and each determination is fact specific. Because class certifications are fact specific, comparisons to other class certification cases is of limited value. In any event, the Court is satisfied that plaintiffs have carried their burden in their motion for class certification.

4. Adequacy of Representation

Rule 23(a)(4) requires that "the representative parties will fairly and adequately protect the interests of the class." Fed.R.Civ.P. 23(a)(4). Adequacy of representation includes both adequacy of named plaintiffs counsel, as well as adequacy of representation in protecting the different, separate, and distinct interests of the class members. *Retired Chi. Police Ass'n*, 7 F.3d at 598. "A class representative must be part of the class and possess the same interest and suffer the same injury as the class members." *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 625-26, 117 S.Ct. 2231, 138 L.Ed.2d 689 (1997).

Plaintiffs claim they have no interest antagonistic to the class. However, defendants argue that plaintiffs claims are in direct conflict with putative members of the class because, in order to prove their damages, plaintiffs must demonstrate that the price was artificial on the dates they purchased the June Contract, while other class members who sold on those same dates would have an interest in demonstrating the price was not artificially high in order to maximize their damages.[3]

The Court is satisfied that the representative parties will fairly and adequately protect the interests of the class. Despite defendants' arguments that there exists a potential conflict of interest in proving various levels of artificiality on different dates throughout the

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[3] Defendants also claim that the allegations of plaintiffs' complaint are partly attributable to one of the putative class members plaintiffs seek to represent. This argument will not preclude certification of the class, though it may be probative during the liability or damages stage of the trial.

class period, courts have rejected similar arguments when certifying classes. *See Fry v. UAL, Corp.*, 136 F.R.D. 626, 633-34 (N.D.Ill.1991) ("[A]ny alleged conflict in the fact [that plaintiffs] were primarily sellers of put contract [that must prove a decrease in price] as opposed to sellers of common stock [that must prove a increase in price] will arise at the damages stage of the litigation,"); *Blackie*, 524 F.2d at 908 (agreeing that at some point in the litigation the class members will have differing interests, i.e., maximizing the inflation existing on one day while minimizing it on other days, but "altogether disagree[ing], for a spate of reasons, that such potential conflicts afford a valid reason at this time for refusing to certify the class."); *In re Natural Gas Commodities Litig.*, 231 F.R.D. at 183 (rejecting argument that class certification is precluded when class members, including purchasers, sellers, and speculators, have potentially conflicting interests in showing defendant's alleged misconduct caused the price to be lower or higher on particular dates). The Court determines that plaintiffs will be adequate representatives and protect the interests of the class. Defendants have failed to dispute adequacy of counsel, and the Court is satisfied that plaintiffs' counsel will vigorously prosecute this case. Accordingly, plaintiffs have fulfilled the adequacy of representation requirement.

The supplemental authority submitted by defendants, *Langbecker v. Elec. Data Sys. Corp.*, 476 F.3d 299 (5th Cir.2007), does not persuade the Court otherwise. *Langbecker* is factually distinguishable from this case because in that case, appellants sought injunctive relief that would have dissolved the stock fund at issue. *Id.* at 315. That stock fund could not be partially dissolved and yet remain open as an

investment option for absent class members, and the appellants were contesting conduct that involved "a multitude of considerations over a period of years." *Id.* In contrast, here, plaintiffs and all class members purchased the exact same standardized futures contract in the same market, seek the same type of relief, and there is a proposed fifty-two-day class period. Therefore, the nature and extent of potential conflicting interests in this case are much less.

B. Rule 23(b) Requirement

In addition to the requirements of Rule 23(a), one of the three subsections of Rule 23(b) must be satisfied before a class may be certified. Fed.R.Civ.P. 23(b), Here, plaintiffs seek certification under Rule 23(b)(3), which requires the court to find that common questions of law or fact "predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy." *Id.*

1. Predominance

The predominance requirement is far more demanding than the commonality requirement of Rule 23(a)(2). *Amchem Prods., Inc.*, 521 U.S. at 623-24, 117 S.Ct. 2231. "At its essence, predominance is concerned with whether the putative named plaintiffs can, through their individualized cases, offer proof on a class-wide basis." *Hyderi v. Wash. Mut. Bank FA*, 235 F.R.D. 390, 398 (N.D.Ill.2006), The court should consider whether the class seeks remedy to a common legal grievance. *Hochschuler*, 82 F.R.D. at 348-49.

Defendants assert that in order to be liable, both the fact of injury and causation must be proven on a class-wide basis. Thus, defendants argue, individual issues regarding whether individual class members

suffered economic losses may predominate over issues common to the class. Additionally, defendants argue that there will be predominant individual issues related to plaintiffs' expert's statistical model and predominant issues raised by class members who satisfied their futures contract obligation with securities rather than cash.

The Court determines that common questions of law will predominate over individual questions. Plaintiffs argue, and the Court agrees, that the predominant issue in this case will be whether defendants unlawfully manipulated prices of the June Contract in violation of the CEA. Accordingly, if plaintiffs can prove price manipulation, then fact of injury will have been established for all members of the class that purchased the June Contract at higher prices than otherwise would have existed absent manipulation. The determination of this legal question involves the same fungible futures contract purchased by all members of the class on the CBT, and the defendants' same alleged manipulative conduct that plaintiffs will attempt to prove through a common economic formula that has been developed through extensive discovery and expert testimony. In sum, the common legal grievance, violation of the CEA, depends upon proof and findings pertaining to defendants' course of conduct and favorable findings would prove the claims of all class members who purchased the June Contract.

Other courts considering class certification for price manipulation claims under the CEA have also found common questions to predominate. *See In re Sumitomo Copper Litig.*, 182 F.R.D. at 90-91 (" 'The common factual questions of the who, what, when, where, and how of the conspiracy, and the common

legal questions of the application of the law, particularly the Commodity Exchange Act, to the facts proven predominate over the individual questions of whether the conspiracy caused each class member some injury.' ") (quoting *Gordon v. Hunt*, 98 F.R.D. 573, 578 (S.D.N.Y.1983)); *see In re Natural Gas Commodities Litig.*, 231 F.R.D. at 183 (stating presence of class members with arguably conflicting interests did not undermine the predominance requirement because all class members have the same shared interest in proving price artificiality). Courts generally focus on the showing of predominance of common questions at the liability stage of litigation rather than at the damages stage. *In re Natural Gas Commodities Litig.*, 231 F.R.D. at 180-81; *Dura-Bilt Corp. v. Chase Manhattan Corp.*, 89 F.R.D. 87, 93 (S.D.N.Y.1981). Thus, the Court rejects defendants' argument that individual questions will predominate because, at some point, damage calculations may be required on an individual basis.[4] For the same reasons,

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[4] Defendants cite the Third Circuit's analysis in *Newton v Merrill Lynch, Pierce Fenner & Smith, Inc.*, 259 F.3d 154 (3rd Cir.2001), as instructive, which involved a § 10(b) claim under the Securities Exchange Act of 1934. The *Newton* court considered the plaintiff's duty to prove that each member of the class was injured by defendant's conduct, as distinguished from calculation of damages. *Id.* at 188. The court stated that class actions based on a fraud-on-the-market theory, excessive securities pricing policies, or antitrust violations were examples of conduct itself causing economic injury, However, the court noted: "[b]ut only those class members whose trades could have been executed at better prices sustained economic injury here," and thus individual questions in determining which class members were harmed was deemed overpowering. *Id.* at 189. In this case, the Court has concluded that injury in fact is satisfied by the fact that class

the Court rejects defendants' arguments related to the plaintiffs' expert's statistical model and class members that satisfied their futures obligations with securities rather than cash as these issues go to the individual determinations of damages after liability has been established. Therefore, the Court determines that plaintiffs have demonstrated that common questions will predominate.

2. Superiority

Rule 23(b)(3) requires "that a class action [be] superior to other available methods for the fair and efficient adjudication of the controversy." Fed.R.Civ.P. 23(b)(3). Defendants argue that many of the putative class members' claims are sufficiently large to provide them with incentive to prosecute their individual claims. Plaintiffs argue that the cost of bringing a commodity futures manipulation action is, even for Breakwater's multi-million dollar claim, a negative value claim—a claim that would cost more to prosecute than may be recovered in damages.

Considering that the size of the potential class is estimated at over one thousand, the class action is a superior method for adjudicating this case. Class actions permit pooled claims that otherwise would be uneconomical to litigate individually to have their day in court. *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 809, 105 S.Ct. 2965, 86 L.Ed.2d 628 (1985). This case involves a large number of investors who are

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members purchased the June Contract at an artificially manipulated high price. This, in essence, is "economic injury" and, thus, the Court does not find *Newton* to be inconsistent with the Court's determination. Moreover, this is not a securities fraud case and, thus, the elements of proof are different.

geographically dispersed and seek to resolve a common legal grievance based on defendants' same course of conduct affecting the same fungible contract purchased on the CBT. The Court determines that judicial resources would be used most efficiently by certifying this class to resolve these common questions.

Additionally, defendants argue that difficulties will be encountered in the management of this class action. Specifically, defendants point to the number of traders within the class and the need for individual determinations of injury. However, previous commodities futures litigation classes have been certified, which were much larger than the class proposed here and included both purchasers and sellers of futures contracts, and were deemed to be manageable. *See, e.g., In re Natural Gas Commodities Litig.*, 231 F.R.D. at 179 (certifying a class numbering in the thousands, including both purchasers and sellers, with a three-year-class period). Therefore, the Court is satisfied that a class action will be a superior method for the fair and efficient adjudication of this controversy.

For the foregoing reasons, the Court finds that all of the requirements for class certification have been satisfied. Accordingly, the Court grants plaintiffs' Amended Motion for Class Certification.

II. Motion to Dismiss

Defendants PIMCO and PIMCO Funds have moved to dismiss the complaint pursuant to Rule 12(b)(6) for failure to state a claim upon which relief can be granted. Under Rule 12(b)(6), a court must "determine whether the complaint contains 'enough factual matter (taken as true)' to provide the minimum notice of the plaintiffs' claim that the Court believes a defendant [is]

entitled to." *In re Ocwen Loan Servicing, LLC Mortg. Servicing Litig.*, 491 F.3d 638, 648-49 (7th Cir.2007) (quoting *Bell Atlantic Corp. v. Twombly*, — U.S. —, — - —, 127 S.Ct. 1955, 1967-69, 167 L.Ed.2d 929 (2007)). All factual allegations and the inferences reasonably arising therefrom are accepted as true. *Gibson v. City of Chi.*, 910 F.2d 1510, 1520-21 (7th Cir.1990). However, the Court is not required to ignore facts in the complaint which undermine a plaintiff's claim. *R.J.R. Servs., Inc. v. Aetna Cas. Sur. Co.*, 895 F.2d 279, 281 (7th Cir.1988).

Price manipulation of a commodity is prohibited by the CEA. 7 U.S.C. §§ 13(a)(2), 25(a). Although not defined in the statute, "broadly stated, [manipulation] is an intentional exaction of a price determined by forces other than supply and demand." *Frey v. Commodity Futures Trading Comm'n*, 931 F.2d 1171, 1175 (7th Cir.1991).[5] The four elements of a price manipulation claim are: "(1) the defendant possessed the ability to influence prices; (2) an artificial price existed; (3) the defendant caused the artificial price; and (4) the defendant specifically intended to cause the artificial price." *In re Soybean Futures Litig.*, 892 F.Supp. at 1045.

A. PIMCO Funds' Motion to Dismiss

The Court first considers PIMCO Funds' arguments in support of its motion to dismiss. First, PIMCO Funds argues it lacked the necessary intent to violate the CEA. PIMCO Funds contends that the

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[5] The *Frey* court noted: "Sophisticated economic justification for the distinctions made in [the price manipulation area] may at times seems questionable. Sometimes the 'know it when you see it' test may appear most useful." *Id.*

complaint alleges PIMCO Funds was "controlled" and "managed" by PIMCO, and PIMCO "caused PIMCO Funds' " conduct in purchasing futures contract positions. (Compl.¶ 23.) Therefore, PIMCO Funds concludes that the complaint itself concedes PIMCO Funds did not have the requisite ability or intent to manipulate the market. Second, PIMCO Funds argues plaintiffs fail to state a claim for aiding and abetting a violation of the CEA. Under § 22 of the CEA, to state a claim for aiding and abetting, plaintiffs must allege PIMCO Funds "(1) had knowledge of the principal's ... intent to commit a violation of the Act; (2) had the intent to further that violation; and (3) committed some act in furtherance of the principal's objective." *See Damato v. Hermanson*, 153 F.3d 464, 473 (7th Cir.1998).

Plaintiffs assert that they have alleged that PIMCO Funds[6] knowingly aided and abetted the violations of the CEA, willfully intended to assist the manipulation, and had the motive and intent to profit from artificial prices. (Compl.¶¶ 92, 104, 105.) Moreover, plaintiffs argue that it is premature to resolve PIMCO Funds' manipulative intent at this stage of the litigation.

Taking all factual allegations and the inferences reasonably arising therefrom as true, the Court concludes that plaintiffs have adequately pleaded that PIMCO Funds had the requisite intent to manipulate prices. Intent is a subjective inquiry and "must of necessity be inferred from the objective facts and may, of course, be inferred by a person's actions and the totality of the circumstances." *In re Ind. Farm Bureau*

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[6] PIMCO and PIMCO Funds are referred to collectively in plaintiffs' complaint. (Compl.¶ 23.)

Coop. Ass'n, Inc., No. 75-14, 1982 WL 30249, at *5 (C.F.T.C. Dec. 17, 1982). *Cf. Makor Issues Rights, Ltd., v. Tellabs, Inc.*, 437 F.3d 588, 602 (7th Cir.2006) (stating, with regard to pleading a securities fraud claim, "[i]f a reasonable person could not draw ... an inference [of scienter] from the alleged facts, the defendants are entitled to dismissal"). Here, considering the totality of the circumstances, it can be reasonably inferred from the facts alleged that PIMCO Funds intended to cause artificial prices or otherwise manipulate the futures market. PIMCO Funds is alleged to have accumulated a very large long position in the June Contract, which it did not liquidate, and PIMCO Funds is alleged to have accumulated a large position in the CTD Note. This coincided with an above average number of deliveries on the June Contract, which could not be satisfied with the CTD Treasury note. The reasonable inference that PIMCO Funds' had the requisite intent is not negated by plaintiffs' reference in the complaint to PIMCO causing PIMCO Funds' conduct because, taking the allegations as true and all reasonable inferences arising therefrom, PIMCO Funds was well aware of its ability to influence prices while it was accumulating these large contract positions. In addition, plaintiffs have sufficiently alleged that PIMCO Funds had the requisite intent with regard to aiding and abetting a violation of the CEA. For the reasons discussed above, it can be reasonably inferred form the alleged facts that PIMCO Funds knew that PIMCO intended to manipulate the futures market by accumulating large positions in the June Contract and the CTD Treasury note, and by acting as the purchaser of such notes, PIMCO Funds intended and actually furthered PIMCO's objective.

Therefore, for the foregoing reasons, the Court denies PIMCO Funds' motion to dismiss.

B. PIMCO and PIMCO Funds' Joint Motion to Dismiss

The Court next considers PIMCO's arguments in support of its motion to dismiss. PIMCO Funds has joined the motion and adopts it in its entirety. (PIMCO Funds' Mem. Supp. Mot. Dismiss 1.)

The first element of a price manipulation claim requires that defendants possess the ability to influence prices. *In re Soybean Futures Litig.*, 892 F.Supp. at 1045. Defendants argue they did not have the ability to manipulate prices because the June Contract allows for delivery of a number of other Treasury notes besides the CTD Treasury note. (Compl.¶¶ 33-34.) In fact, defendants assert that they only held 3.16% of the notes deliverable under the terms of the June Contract. (PIMCO's Mem. Supp. Mot. Dismiss 6.) In support of this argument, defendants cite the Commodity Futures Trading Commission ("CFTC") in *In re Cox:* "the terms of the underlying futures contract should not be lightly ignored when calculating deliverable supply. If the terms of the contract permit delivery of premium grades of the commodity, then premium grades must be counted as part of the relevant supply, if otherwise available." No. 75-16, 1987 CFTC Lexis 325, at *20 (C.F.T.C. July 15, 1987). Therefore, defendants contend, June Contract prices could not have been artificial because the price was based on a mix of notes that are expressly deliverable under the terms of the June Contract.

Plaintiffs contend that defendants' argument has been refuted by the CFTC in *In re Fenchurch Capital*

Management, Ltd. The CFTC found that Fenchurch controlled a dominant portion of the available supply of the CTD Treasury note but acknowledged that the terms of the futures contract allowed for delivery of securities other than the CTD Treasury note. No. 96-7, 1996 WL 382313, at *6 (C.F.T.C. July 10, 1996). However, the CFTC stated that the pricing and delivery system at issue (*i.e.*, Treasury note futures) was different from that in *In re Cox* (*i.e.*, wheat futures), which led the CFTC to conclude Fenchurch's exacerbating conduct of increasing its position in the CTD Treasury note constituted manipulation in violation of the CEA, which resulted in certain shorts delivering a more valuable security. *Id.*

However, defendants contend *In re Fenchurch* is distinguishable from this case. The alleged manipulative conduct in *In re Fenchurch* commenced after trading on the futures contract had expired. *Id.* In contrast, here, the alleged misconduct occurred while the June Contract was still trading, and defendants argue the price of the June Contract reflected the current supply of the various contracts available for delivery, which absolves defendants from having the requisite ability to manipulate prices. Plaintiffs reply by arguing that the CFTC in *In re Fenchurch* intended its analysis to apply to futures contracts on treasury securities.[7]

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[7] The CFTC stated in *In re Fenchurch*:

> Further, the Commission does not intend that its determination that Fenchurch controlled the available deliverable supply of the Ten-Year Treasury note contracts by dominating a portion of that supply (i.e., control of the cheapest-to-deliver notes) necessarily should apply in

Notwithstanding the intricacies of these arguments, plaintiffs have alleged defendants accumulated an unprecedented long position in the June Contract, which it did not liquidate, and a large position in the CTD Treasury note. Even if the Court were to accept the reasoning in *In re Cox* and defendants' argument that the price of the June Contract reflected the availability of all the notes available for delivery under the express terms of the June Contract, the price of the June Contract could still have been manipulated by defendants' alleged conduct because the June Contract, as defendants argue, incorporated the short supply of the CTD Treasury note available in the market. Therefore, defendants' large accumulation of the CTD Treasury note could have provided them with the ability to influence the price of the June Contract.

Moreover, regardless of the timing of purchases in *In re Fenchurch*, implicit in the CFTC's analysis was that Fenchurch's activity of increasing its position in the CTD Note gave Fenchurch the ability to influence prices of the futures contract. 1996 WL 382313, at *5 ("Fenchurch ... controlled a dominant portion of the cheapest-to-deliver notes ... and thus restricted the available supply of the cheapest-to-deliver issue. Fenchurch's conduct resulted in the value of the futures contract being artificially altered."). It is notable that the CBT announced on June 29, 2005 that it was amending CBT Regulation 425.01 to limit the permissible Ten-Year Treasury note contract position to 50,000 contracts during the last ten trading days.

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determining available deliverable supply in markets other than those for futures on treasury securities.

1996 WL 382313, at *6.

(Compl.¶ 81.) Plaintiffs allege that 50,000 contracts is one-third of the amount defendants held, a fact the Court assumes is true for the purposes of this motion, and that the CBT's amended rule implies that a 50,000 contract position could create an ability to cause artificial prices. Therefore, the Court is satisfied that plaintiffs have adequately pleaded that defendants possessed the ability to influence prices of the June Contract.

The second and third elements of a price manipulation claim require plaintiffs to prove that an artificial price existed and that defendants caused the artificial price. *In re Soybean Futures Litig.*, 892 F.Supp. at 1045. Plaintiffs allegations are sufficient to satisfy their burden of pleading the existence of an artificial price caused by defendants' conduct for the same reasons the Court found plaintiffs adequately pleaded that defendants had the ability to manipulate prices. Also, for these same reasons, the Court rejects defendants' argument that the price was not artificial because the price reflected the availability of all the contracts available for delivery under the express terms of the June Contract.

The fourth element of a price manipulation claim requires the allegation that defendants specifically intended to cause the artificial price. *In re Soybean Futures Litig.*, 892 F.Supp. at 1045. Plaintiffs must allege that defendants both intentionally acquired the ability to manipulate prices and thereafter exercised that ability to cause artificial prices. *See In re Ind. Farm Bureau Coop. Ass'n, Inc.*, 1982 WL 30249, at *8 n. 13 (citing *Volkart Bros., Inc. v. Freeman*, 311 F.2d 52, 58-59 (5th Cir.1962); *Cargill, Inc. v. Hardin*, 452 F.2d 1154, 1163 (8th Cir.1971)). Defendants argue that plaintiffs' claim fails because the complaint does not

allege defendants acquired its contract position with the intent to create artificial prices. Rather, plaintiffs merely allege an intentional breach of a duty by failing to liquidate its long positions.

Plaintiffs contend that the complaint alleges defendants intended to cause artificial prices. Specifically, plaintiffs allege that defendants: (1) "knowingly" changed their behavior as the futures contracts became susceptible to manipulation by persons controlling a large long position by their acts of acquiring an "extraordinary large long position" and refusing to liquidate (Compl.¶¶ 1-4, 52-53, 60, 75); (2) were well aware of this form of manipulation (*id.* ¶¶ 41-45); (3) the motive and intent for the manipulative acts described in the complaint was to increase financial return (*id.* ¶ 92); and (4) intended to and did manipulate prices of the June Contract during the class period (*id.* ¶ 13.).

As discussed above, intent is a subjective inquiry and thus may be inferred from the facts alleged and the totality of the circumstances. *In re Ind. Farm Bureau Coop. Ass'n, Inc.*, 1982 WL 30249, at *5. Accepting plaintiffs' factual allegations as true, and drawing all reasonable inferences in their favor, the Court is persuaded that plaintiffs have adequately pleaded that defendants intended, at the time of acquisition, to cause an artificial price and subsequently exercised the ability to influence prices. Considering the totality of the circumstances, it may be reasonably inferred that defendants intended to acquire a very large long position in the June Contract and a large position in the CTD Treasury note because defendarts would be benefited by refraining from liquidating these positions and instead taking delivery of more valuable notes other than the CTD Treasury note. Moreover, in a

market that was susceptible to manipulation by a dominant long position, it is reasonable to infer that defendants were well aware of their potential ability to influence prices and that they intended to manipulate the futures market at the time of acquisition of the large contract positions.

Plaintiffs argue in the alternative that even if defendants did not intend to manipulate prices when they acquired their contract positions, they are liable once the requisite intent developed. Plaintiffs cite *Fenchurch*, in which the CFTC stated: "the Commission has held that even if a dominant long played no role in the creation of a congested market, the long has a duty to avoid conduct that exacerbates the situation." 1996 WL 382313, at *6. Plaintiffs have alleged defendants intentionally exacerbated the market, which was susceptible to price manipulation. (Compl. ¶ 11.)

Defendants assert that a mere refusal to liquidate is not the type of affirmative exacerbation that other courts have relied upon. Defendants argue that the type of manipulative intent that would suffice is conduct summarized in *In re Indiana Farm Bureau Cooperative Association, Inc.* "Manipulative intent may be inferred ... where, once the congested situation becomes known to him, the long exacerbates the situation by, for example, intentionally decreasing the cash supply or increasing his long position in the futures market." 1982 WL 30249, at *8 n. 12.

Although *In re Indiana Farm Bureau Cooperative Association, Inc.* set forth two situations in which manipulative intent may be inferred, the list is by no means exclusive. *See Cargill, Inc. v. Hardin*, 452 F.2d 1154, 1163 (8th Cir.1971) ("The methods and techniques of manipulation are limited only by the ingenuity of

man."). Considering the totality of the circumstances, intentional exacerbating conduct may be reasonably inferred from the alleged fact that defendants sold their entire position in the CTD Treasury note by September 30, 2005, mere months after purportedly accumulating these notes for investment purposes. Therefore, for the foregoing reasons, the Court is satisfied that plaintiffs have adequately alleged that defendants intended to cause an artificial price of the June Contract. Accordingly, the Court finds that plaintiffs have sufficiently pleaded their claims that defendants violated the CEA.

Finally, defendants argue that all claims against John Doe defendants should be dismissed for failure to state causes of action against such defendants. Plaintiffs do not oppose the dismissal, (Pls.' Mem. Opp'n PIMCO's Mot. Dismiss 25 n. 17), and thus the Court grants defendants motion to dismiss as to the John Doe allegations.

Conclusion

For the foregoing reasons, the Court grants Plaintiffs First Amended Motion for Class Certification, [doc. no. 87], denies PIMCO Funds' motion to dismiss, [doc. no. 82], grants PIMCO's Motion to Dismiss (which PIMCO Funds has joined) as to the John Doe allegations and denies the remainder of PIMCO's motion to dismiss [doc. no. 85].

SO ORDERED.

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

December 10, 2007

Before

Hon. MICHAEL S. KANNE, *Circuit Judge*

Hon. DIANE P. WOOD, *Circuit Judge*

Hon. DIANE S. SYKES, *Circuit Judge*

IN RE:	]	Petition for Permission
PACIFIC	]	to Appeal Pursuant to
INVESTMENT	]	F.R.C.P. 23(f), Northern
MANAGEMENT	]	District of Illinois,
COMPANY and	]	Eastern Division
PIMCO FUNDS,	]	
Petitioners.	]	No. 05 C 4681
	]	
No. 07-8024	]	Ronald A. Guzman,
	]	Judge.

The following are before the court:

1. **PETITION FOR PERMISSION TO APPEAL PURSUANT TO RULE 23(f) OF THE FEDERAL RULES OF CIVIL PROCEDURE FROM ORDER GRANTING CLASS CERTIFICATION**, filed on August 14, 2007, by counsel for the petitioners.
2. **RESPONDENTS' ANSWER IN OPPOSITION TO THE RULE 23(f) PETITION OF DEFENDANTS FOR**

LEAVE TO APPEAL THE DISTRICT COURT'S CLASS CERTIFICATION ORDER FILED UNDER SEAL, filed on August 30, 2007, by counsel for the respondents.

3. **RESPONDENTS' MOTION FOR LEAVE TO FILE UNDER SEAL A PORTION OF THEIR ANSWER IN OPPOSITION TO THE RULE 23(f) PETITION OF DEFENDANTS FOR LEAVE TO APPEAL THE DISTRICT COURT'S CLASS CERTIFICATION ORDER,** filed on August 30, 2007, by counsel for the respondents.

IT IS ORDERED that #1 is **GRANTED.** Petitioners shall pay the required appellate fees to the clerk of the district court within 10 days from the entry of this order pursuant to Fed. R. App. P. 5(d)(1). Once the district court notifies this court that the fees have been paid, the appeal will be entered on this court's general docket.

IT IS FURTHER ORDERED that #3 is **DENIED.** The clerk shall file the unredacted version of #2 **INSTANTER** and this document shall become part of the public record.

A True Copy
[illegible]
/s/
Clerk of the United States
Court of Appeals for the
Seventh Circuit

[notary seal omitted]

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

July 31, 2009

Before

Richard A. Posner, *Circuit Judge*

Terence T. Posner, *Circuit Judge*

John Daniel Tinder, *Circuit Judge*

No. 08-1075

JOSEF A. KOHEN, *et al.*, on their own behalf and that of all others similarly situated,
Plaintiffs-Appellees

v.

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC and PIMCO FUNDS,
Defendants-Appellants

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division

No. 05 C 4681

Ronald A. Guzman, *Judge.*

ORDER

On July 21, 2009, defendant-appellant Pacific Investment Management Company LLC filed a

petition for rehearing and petition for rehearing *en banc*. All the judges on the original panel have voted to deny the petition, and none of the active judges has requested a vote on the petition for rehearing *en banc*.* The petition is therefore DENIED.

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* Circuit Judge Ilana Diamond Rovner did not participate in the consideration of this petition for rehearing.

United States Code Annotated
Title 7. Agriculture
Chapter 1. Commodity Exchanges

7 U.S.C. § 13

§ 13. Violations generally; punishment; costs of prosecution

(a) Felonies generally

It shall be a felony punishable by a fine of not more than $1,000,000 or imprisonment for not more than 10 years, or both, together with the costs of prosecution, for:

* * *

(2) Any person to manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, or to corner or attempt to corner any such commodity or knowingly to deliver or cause to be delivered for transmission through the mails or interstate commerce by telegraph, telephone, wireless, or other means of communication false or misleading or knowingly inaccurate reports concerning crop or market information or conditions that affect or tend to affect the price of any commodity in interstate commerce, or knowingly to violate the provisions of section 6, section 6b, subsections (a) through (e) of[1] subsection 6c, section 6h, section 6*o*(1), or section 23 of this title.

* * *

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[1] So in original. Probably should be "section".

United States Code Annotated
Title 7. Agriculture
Chapter 1. Commodity Exchanges

7 U.S.C. § 25

§ 25. Private rights of action

(a) Actual damages; actionable transactions; exclusive remedy

(1) Any person (other than a registered entity or registered futures association) who violates this chapter or who willfully aids, abets, counsels, induces, or procures the commission of a violation of this chapter shall be liable for actual damages resulting from one or more of the transactions referred to in subparagraphs (A) through (D) of this paragraph and caused by such violation to any other person—

(A) who received trading advice from such person for a fee;

(B) who made through such person any contract of sale of any commodity for future delivery (or option on such contract or any commodity); or who deposited with or paid to such person money, securities, or property (or incurred debt in lieu thereof) in connection with any order to make such contract;

(C) who purchased from or sold to such person or placed through such person an order for the purchase or sale of—

(i) an option subject to section 6c of this title (other than an option purchased or sold on a registered entity or other board of trade);

(ii) a contract subject to section 23 of this title; or

(iii) an interest or participation in a commodity pool; or

(D) who purchased or sold a contract referred to in subparagraph (B) hereof if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract.

(2) Except as provided in subsection (b) of this section, the rights of action authorized by this subsection and by sections 7(d)(13), 7a-1(c)(2)(H), and 21(b)(10) of this title shall be the exclusive remedies under this chapter available to any person who sustains loss as a result of any alleged violation of this chapter. Nothing in this subsection shall limit or abridge the rights of the parties to agree in advance of a dispute upon any forum for resolving claims under this section, including arbitration.

(3) In any action arising from a violation in the execution of an order on the floor of a registered entity, the person referred to in paragraph (1) shall be liable for—

(A) actual damages proximately caused by such violation. If an award of actual damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under section 2(a)(1) of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award; and

(B) where the violation is willful and intentional, punitive or exemplary damages equal to no more

than two times the amount of such actual damages. If an award of punitive or exemplary damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under section 2(a)(1) of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award if the floor broker fails to do so, except that such requirement shall apply to the futures commission merchant only if it willfully and intentionally selected the floor broker with the intent to assist or facilitate the floor broker's violation.

* * *

United States Code Annotated
Title 28. Judiciary and Judicial Procedure
Part V. Procedure
Chapter 131. Rules of Courts

28 U.S.C. § 2072

§ 2072. Rules of procedure and evidence; power to prescribe

(a) The Supreme Court shall have the power to prescribe general rules of practice and procedure and rules of evidence for cases in the United States district courts (including proceedings before magistrate judges thereof) and courts of appeals.

(b) Such rules shall not abridge, enlarge or modify any substantive right. All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect.

(c) Such rules may define when a ruling of a district court is final for the purposes of appeal under section 1291 of this title.

FEDERAL RULE OF CIVIL PROCEDURE FOR THE UNITED STATES DISTRICT COURTS

Title IV. Parties

Rule 23. Class Actions

(a) **Prerequisites.** One or more members of a class may sue or be sued as representative parties on behalf of all members only if:

(1) the class is so numerous that joinder of all members is impracticable;

(2) there are questions of law or fact common to the class;

(3) the claims or defenses of the representative parties are typical of the claims or defenses of the class; and

(4) the representative parties will fairly and adequately protect the interests of the class.

(b) **Types of Class Actions.** A class action may be maintained if Rule 23(a) is satisfied and if:

(1) prosecuting separate actions by or against individual class members would create a risk of:

(A) inconsistent or varying adjudications with respect to individual class members that would establish incompatible standards of conduct for the party opposing the class; or

(B) adjudications with respect to individual class members that, as a practical matter, would be dispositive of the interests of the other members not parties to the individual adjudications or would substantially impair or impede their ability to protect their interests;

(2) the party opposing the class has acted or refused to act on grounds that apply generally to the class, so that final injunctive relief or corresponding declaratory relief is appropriate respecting the class as a whole; or

(3) the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for fairly and efficiently adjudicating the controversy. The matters pertinent to these findings include:

(A) the class members' interests in individually controlling the prosecution or defense of separate actions;

(B) the extent and nature of any litigation concerning the controversy already begun by or against class members;

(C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and

(D) the likely difficulties in managing a class action.

* * *

[Text of subdivision (f) effective until December 1, 2009, absent contrary Congressional action.]

(f) **Appeals.** A court of appeals may permit an appeal from an order granting or denying class-action certification under this rule if a petition for permission to appeal is filed with the circuit clerk within 10 days after the order is entered. An appeal does not stay proceedings in the district court unless the district judge or the court of appeals so orders.

[Text of subdivision (f) effective December 1, 2009, absent contrary Congressional action.]

(f) **Appeals.** A court of appeals may permit an appeal from an order granting or denying class-action certification under this rule if a petition for permission to appeal is filed with the circuit clerk within 14 days after the order is entered. An appeal does not stay proceedings in the district court unless the district judge or the court of appeals so orders.

* * *

Figure 1 Total Richness of June 2005 10-Year Treasury Futures Contract
(with 95% confidence one-tailed artificial richness test bound)

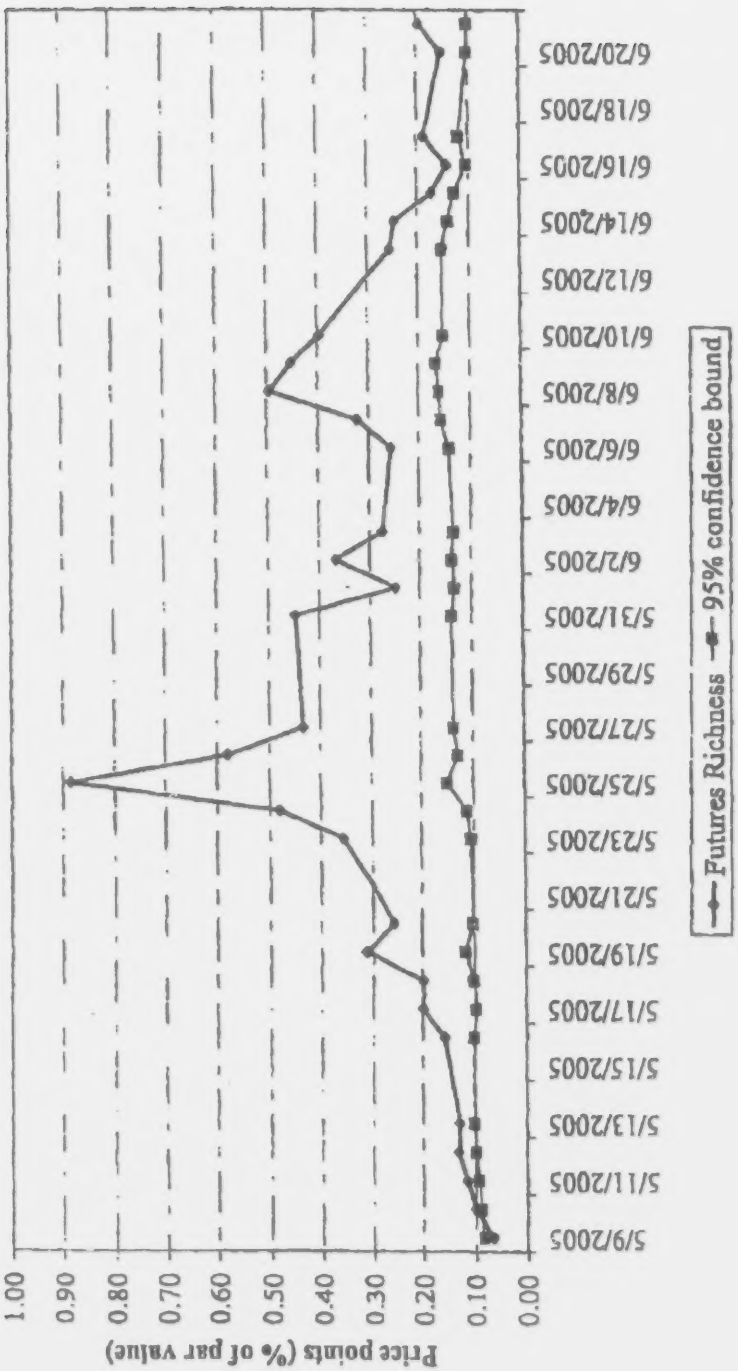

Exhibit 9

20050509	0.1108
20050510	0.1517
20050511	0.2033
20050512	0.1936
20050513	0.1666
20050516	0.1750
20050517	0.1799
20050518	0.2802
20050519	0.2897
20050520	0.4320
20050523	0.4662
20050524	0.7339
20050525	0.6782
20050526	0.4928
20050527	0.5207
20050531	0.2625
20050601	0.2328
20050602	0.3010
20050603	0.2734
20050606	0.2956
20050607	0.4106
20050608	0.4320
20050609	0.3394
20050610	0.3010
20050613	0.2200
20050614	0.1586
20050615	0.1518
20050616	0.2317
20050617	0.1578
20050620	0.1467
20050621	0.3073

Supreme Court, U.S.
FILED
JAN 14 2010
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No. 09-517

In The Supreme Court of the United States

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC, et al.,

Petitioners,

v.

RICHARD HERSHEY, et al.,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

In a class action alleging manipulation in violation of the Commodity Exchange Act ("CEA"), 7 U.S.C. §§ 1, *et seq.*, the Plaintiffs' final merits expert report on liability and damages was submitted by the Defendants in a surreply filing on the FRCP Rule 23 motion to certify the action as a class action.

Plaintiffs' merits expert report provided evidence that all class members paid artificially high prices to buy out of their short futures contract positions. Defendants conceded that all class members had Constitutional injury and standing. But Defendants nonetheless assert that certain class members are supposedly "uninjured" because, unlike with statutory standing principles generally, Section 22 (a) of the CEA, 7 U.S.C. §25(a), supposedly superimposes on the CEA statutory standing analysis a requirement that actual damages be proved.

Question #1. Does Section 22(a) of the Commodity Exchange Act require proof of actual damages in order to establish statutory injury and standing under the CEA?

In an interlocutory review of the inherently conditional FRCP Rule 23 order on a motion for class certification, the Seventh Circuit Court of Appeals found no abuse of discretion or legal error in the District Court's specific findings and rigorous analysis concluding that Plaintiffs had proved all of the required elements of Rule 23(a) and Rule 23(b)(3).

On the Class motion, Defendants conceded that class counsel was "adequate" to represent the class

under Rule 23(a)(4). Defendants also conceded during the Seventh Circuit oral argument that the action was a proper class action to the extent of persons who sold prior to the first day of the Class Period. But Defendants argue, contrary to all Circuit court decisions, including the Decision below, that this particular class that included both buyers and sellers did not have adequate representation.

Question #2. Did the Seventh Circuit Court of Appeals erroneously refuse to modify the scope of the class by holding that the District Court did not abuse its discretion in finding "adequacy" under Rule 23(a)(4) in the representation of the class that included certain members who both purchased and sold?

PARTIES TO THE PROCEEDING

The Petition (p. ii) lists the individual and the corporations that are now parties to this proceeding.

Pursuant to Rule 29.6, respondent Breakwater Trading LLC states that it is a limited liability corporation, wholly owned by Breakwater Capital, LLC. Breakwater Capital LLC is in turn owned by 20 individual shareholders. Breakwater Trading LLC states further that no publicly held company owns 10% or more of its stock.

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REASONS FOR DENYING CERTIORARI

This is an appeal of an interlocutory class certification order. Review of such interlocutory orders by way of writ of certiorari is ordinarily inappropriate. See, *e.g.*, *American Construction Co, v. Jacksonville T. & K. W. Railway Co.*, 148 U.S. 372, 384 (1893); *Virginia Military Institute v. United States*, 508 U.S. 946 (1993). This is particularly true of class certification orders, that are themselves conditional, and "subject to revision in the District Court". Fed. R. Civ. P. 23(c)(1); *Coopers and Lybrand v. Livesay*, 437 U.S. 463, 469 (1978).

The inherently fact-bound Rule 23 determination in this case does not conflict with any decision of this Court or any other Court of Appeals. It is Petitioner-Defendants' ("Defendants") arguments, not the Seventh Circuit Court of Appeals opinion ("Decision"), which are in conflict with other Circuits.

Class actions alleging manipulation of prices in the "esoteric"[1] commodity futures markets are exceedingly rare, averaging less than one per year for the last thirty-five years. Argument "E" *infra*.

Unlike the federal securities laws, Congress has never criticized, limited or sought to impose a "reform" experiment on class actions or other actions under the Commodity Exchange Act, 7 U.S.C. §1 *et seq*. ("CEA").

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[1] Commodity futures trading is "esoteric." *Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 356 (1982) quoting H.R. Rep. No. 93-975, p. 1 (1974), 1974 U.S. Code Cong & Admin. News at 5843.

Compare CEA *passim* Section 7 U.S.C. § 25(a) *with* the Private Securities Litigation Reform Act of 1995, Pub. L. 104-67, 109 Stat. 737 (codified as amended in various sections of 15 U.S.C.).

On the contrary, private actions are "critical" to deterring manipulation in the commodity futures markets which have been plagued by manipulation and "bubbles" in recent years. Counterstatement of The Case "B" and Argument "E" *infra*.

Interlocutory review seeking to modify what Defendants conceded at oral argument in the Seventh Circuit Court of Appeals was a substantially proper class definition, is unwarranted and would address no important questions concerning the inherently conditional Rule 23 class certification order.

Contrary to the premise for Defendants' arguments, the Decision does not inject "uninjured" persons into the class nor otherwise conflict with the decisions of this Court or other Circuits or the requirements of the Rules Enabling Act, 28 U.S.C. §§2071-2077. *Compare* Defendants' Petition for a Writ of Certiorari dated October 30, 2009 ("Pet.") at 11-17. Rather, Defendants seriously misinterpret Section 22(a) of the CEA, 7 U.S.C. §25(a), Plaintiffs' merits expert report, and the Decision itself.

Injury. Plaintiffs' merits expert reports provided extensive evidence that Defendants committed multiple manipulative acts which caused artificially high prices throughout the Class Period. Seventh Circuit Court of Appeals Separate Appendix of Appellees ("S.Appx.") at 144-5.

If accepted by the finder of fact, this expert evidence established that all Class members suffered the injury of paying artificially high prices to buy out of their short positions in futures contracts. *Compare* S.Appx.144-5.

Defendants themselves submitted Plaintiffs' merits expert report as part of Defendants' surreply on the class certification motion.

Because of this demonstrated "injury", Defendants expressly concede that all Class members have Constitutional injury and standing. Pet.7.

Statutory Standing. Although they conceded such injury, Defendants nonetheless argue that Section 22(a) of the CEA deprives certain Class members of CEA statutory standing and injury.[2] Specifically, Defendants misinterpret Plaintiffs' expert report to show that certain of such concededly injured Class members who sold after May 9, 2005 will supposedly be found (at or after trial) to have received more price artificiality on their sale of June Contracts than they paid on their liquidating purchase of same. Pet.12.

Defendants argue that this means that these Class members (a) should not receive any damages, and (b)

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[2] Defendants did not raise their present, contrived statutory standing argument in the District Court, including on their motions to dismiss, their motions for summary judgment, nor their oppositions or surreply on class certification.

Instead all that Defendants argued was that certain named Plaintiffs lacked statutory standing because they traded in joint accounts.

moreover, should be **retroactively** regarded as having **lacked CEA statutory standing and injury** under Section 22(a) of the CEA from the outset of the action. Pet.11,15-17.

Compounding their foregoing errors, Defendants misinterpret the Decision as accepting that the foregoing Class members were "uninjured" but nonetheless deciding to allow them to remain within the defined Class and thereby enlarge their substantive rights in violation of the Rules Enabling Act and the decisions of this Court. *Id.*

First, the Decision did **not** use the word "uninjured". Decision *passim*. Second, the Decision did **not** find that there were uninjured Class members. *Id.* Third, the Decision clearly did **not** hold that, even though some Class members supposedly lack statutory standing and injury under the CEA, the Rule 23 class motion device enlarges their substantive rights here. *Compare, id. with* Pet.15-19.

On the contrary, the Decision expressly held that **statutory** standing "refers to a situation in which, although the plaintiff has been injured and would benefit from a favorable judgment and so has standing in the Article III sense, he is suing under a statute that was not intended to give him a right to sue; he is not within the class intended to be protected by it." Appendix to Defendants' Petition for a Writ of Certiorari dated October 30, 2009 ("Pet.App.") at 10a. And, notwithstanding Defendants' elaborate argument under Section 22(a) of the CEA, the Decision correctly found that "this is not such a case." *Id.*

Because the Decision rejects Defendants' "Class members lack CEA statutory standing and injury" premise for Defendants' "uninjured" Class members argument, the Decision does not purport to expand any Class members' substantive rights and clearly does not conflict with this Court's precedent or the Rules Enabling Act, 28 U.S.C. §§ 2071–2077. *Id.*

Instead, the Decision applied such precedent to Plaintiffs' final merits expert report and the other specific facts and context here, including Section 22(a) of the CEA. Thus, Defendants' stated reasons for granting certiorari are non-existent. Any review of the Decision will devolve into an analysis of Defendants' arguments under Section 22(a) of the CEA, Defendants' misinterpretations of Plaintiffs' merits expert report, and the "esoterics" of open interest and other aspects of the commodity futures market.

COUNTERSTATEMENT OF THE CASE

A. The *Raison D'Être* For The Commodity Exchange Act Is The Prevention of Price Manipulation

The commodity futures markets provide the benefits of "the stabilization of commodity prices, the provision of reliable pricing information, and the insurance against loss from price fluctuation." *Cargill, Inc. v. Hardin*, 452 F.2d 1154, 1173 (8th Cir. 1971), *cert. denied sub nom. Cargill v. Butz*, 406 U.S. 932 (1972).

Price manipulation destroys all of these benefits. *Id.* Therefore, Congress **unqualifiedly** prohibits price manipulation in the futures markets. *Compare, Strobl*

v. New York Mercantile Exchange, 768 F.2d 22, 28 (2d Cir. 1985) ("a little manipulation" is permitted under the federal securities laws but all manipulation is prohibited under the CEA, 7 U.S.C. §1, *et seq.*).

Indeed, Congress' *raison d'être* for originally enacting and repeatedly enhancing the CEA has been to prevent, and provide ample avenues of redress for, futures price manipulation by "big traders."[3]

B. Congress Considered Private Rights of Action To Be "Critical" In Preventing Price Manipulation

Congress viewed private lawsuits as:

> **Critical** to protecting the public and fundamental to maintaining the credibility of the futures market.

[Emphasis is supplied in all quotes herein unless otherwise noted.] *Cange v. Stotler & Co.*, 826 F.2d 581, 594-595 (7th Cir. 1987) (*citing* to H.R. Rep. No. 565, 97th Cong., 2d Sess., pt. 1 at 56-7, *reprinted* in 1982 U.S. Code Cong. & Admin. News 3871, 3905-06); *accord, Merrill Lynch v. Curran*, 456 U.S. at 384-5 ("valuable supplement" to regulation).

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[3] *Compare Leist v. Simplot*, 638 F.2d 283, 304-6 n.24 (2d Cir. 1980) (Friendly, J.), *aff'd, Merrill Lynch Fenner & Smith v. Curran*, 456 U.S. 353, 384-85 (1982) ("*Merrill Lynch v. Curran*") *and* Section 3 of the CEA, 7 U.S.C. § 5 (core purpose of the CEA is "to deter and prevent price manipulation or any other disruptions to market integrity") *with Board of Trade v. Olsen*, 262 U.S. 1, 39 (1923) ("futures market lends itself to such manipulation much more readily than a cash market").

C. The Regulators In This Case Warned Defendants That They Would Face Private Law Suits If Defendants Did Not Stop Their Uneconomic Conduct

Indeed, Defendants were expressly warned by the regulators from the Chicago Board of Trade ("CBOT") that Defendants were engaged in uneconomic conduct in the June 2005 10-year U.S. Treasury note futures contracts ("June Contracts") that would lead to lawsuits by the "shorts"[4] in these contracts if Defendants did not stop. S.Appx.149,214; Declaration of Christopher McGrath ("M.Decl."), *Kohen v. Pacific Investment Management Co. LLC.*, No. 05 C 4681 (N.D. Ill., filed Dec 6, 2007) [Docket No. 346], Ex 120 at pp. 174-5.

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[4] "A commodity futures contract is simply a [standardized] bilateral executory agreement for the purchase and sale of a particular commodity." *Leist*, 638 F.2d at 322.

The "bilateral" aspect of the futures contract is that there is a seller and buyer. *Id.* The "executory" aspect is that the seller agrees that it will sell and the buyer agrees that it will buy, during a specific month in the future, the specified quantity and quality of the specified commodity at the price established by their respective trades on (in this case) the CBOT. *Id.*

The sellers are one-half of the bilateral futures contract and one-half of the commodity futures market. *Id.* They are referred to as "shorts." *Id.* The buyers are the other one-half, and are referred to as "longs." *Id.* The standardized futures contracts are written so that both sides owe their obligations to the clearing house of the exchange. *Id.*

D. Flouting Those Warnings, Defendants Made In Excess Of $1,000,000,000 In Profits And Engaged In Extensive Uneconomic Conduct That Artificially Inflated Prices To Five Times Higher Than The Previous All-Time Record

Flouting such warnings from the regulators, Defendants continued their uneconomic conduct and made over $1,000,000,000 in trading profits. Reply Memorandum In Support of Motion to Certify Class *Kohen v. Pacific Investment Management Co. LLC*, No. 05 C 4681 (N.D.Ill., filed Aug. 30, 2006) [Docket No. 126 at p.9].

Defendants purchased up to 87.26% of the long positions in the June Contract. M.Decl. Ex. 136.

Defendants purchased up to 42.46% of the deliverable supply of notes to satisfy long positions on such June Contracts. *Compare,* M.Decl. at Ex. 136 *with* Pet.App. 19a-20a *and In Re Matter of Fenchurch Capital Mgmt., Ltd.*, C.F.T.C. No. 96-7, 1996 WL 382313 (CFTC July 10, 1996) (for CBOT financial futures contracts, the deliverable supply is the portion of the cheapest to deliver ("CTD") note that is "readily available" to be delivered).

Defendants uneconomically demanded all-time record deliveries of 132,493 June Contracts, representing 93.1% of the total contract deliveries. M.Decl. Ex. 136; S.Appx.146-7.

No reported case of which Plaintiffs are aware has ever exonerated an alleged commodity futures manipulator who purchased percentages of the

markets even remotely approaching the levels that Defendants engrossed here.[5]

Moreover, Defendants' conduct intentionally went beyond manipulation. Section 9(a)(2) of the CEA, 7 U.S.C. §13(a)(2), makes it a **felony** (1) to **manipulate**, (2) to **corner**, or (3) to make **false reports** concerning a commodity.

A corner is "...in the **extreme** situation, obtaining contracts requiring the delivery of more commodities than are available for delivery." Commodity Futures Trading Commission ("CFTC") Glossary, available at http://www.cftc.gov/educationcenter/glossary/glossary_co.html (last visited on Jan. 14, 2010).

This is precisely what Defendants achieved during the May 9 – June 21, 2005 Class Period: Defendants' large purchases provided Defendants, by May 24, 2005, with long futures positions calling for almost three times more deliverable notes than existed in the deliverable supply of notes that were not already owned by Defendants. *Compare,* M.Decl. Exs. 136,139 *with* S.Appx.197 (readily available deliverable supply of notes estimated at $15 billion).

According to Plaintiffs' expert, Defendants' extensive uneconomic conduct caused extraordinary,

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[5] *Compare, e.g., Cargill,* 452 F.2d at 1160 (long futures holder manipulated with 24% of deliverable supply); *G. H. Miller & Co. v. United States,* 260 F.2d 286, 289 (7th Cir. 1958) (72.1% of deliverable supply); *In re Landon v. Butler,* 14 A.D. 429 (CEA No. 65, June 20, 1955) (21% of deliverable supply); *Great Western Food Distributors v. Brannan,* 201 F.2d 476, 481 (7th Cir. 1953) (29.3% of deliverable supply).

artificial increases in futures prices. S.Appx.144-5, 207. The June Contract prices reached all-time record levels of richness the first day of the Class Period and continued to inflate until, by May 24-25, the richness was five times higher than the all-time record prior to the Class Period. S.Appx.207; *compare,* M.Decl. Ex. 174 *with* M.Decl. Ex. 66.

Defendants' e-mail record contradicts their sworn testimony. The e-mails reflect, among other things, that Defendants specifically intended to force the shorts in the June Contract to make what Defendants knew were uneconomic deliveries or pay what Defendants themselves said were artificially high prices to buy out of their June Contract short positions. *Compare,* M.Decl. Ex. 119 at pp.235-36 *with* M.Decl. Ex. 50; *see also* S.Appx.167.

E. The Class of Short Traders Suffered The Injury Of Paying The Artificially High Prices That Defendants' Manipulation Caused, In Order To Buy Out Of Their Short Positions

In practice, deliveries on futures contracts are very rare. *Compare,* August 10, 2005 CBOT letter to the Futures Industry Association at p. 1, S.Appx.138 (futures market is not a substitute for the physical delivery market) *with* S.Appx.7, 137 and *Leist,* 638 F.2d at 283, n.2. More than 99% of futures contracts are satisfied by trading to liquidate. *Id.* That is, prior to the expiration of trading in the futures contract, market participants who initially had sold a contract (the so-called "shorts") will buy a contract. S.Appx.7.

This expectation of liquidation on 99-plus% of futures trades permits the liquidity and volume needed for a successful futures contract.[6] This is because persons who do not own or desire to own the specific underlying deliverable instrument, may nonetheless trade the futures contract for many different purposes.

The foregoing great imbalance in commodity futures trading --- in which only a few deliveries discipline an extraordinary trading volume --- is predicated upon the convergence of the price of the futures contract with the price of the deliverable instrument as the end of trading nears. S.Appx.138-9.

However, during the period when the open interest[7] was declining and convergence should have been occurring in the June Contract, Defendants' extensive

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[6] Wholly unlike investors in a stock corporation, trading in each commodity futures contract has a fixed end date by which all traders who have come into the contract must go out of it (or, in extremely rare instances, perform their delivery obligations).

The stock market expects that every trader will actually own or have borrowed (the seller) or actually receive (the buyer) a share of the stock. The commodity futures market makes the opposite expectation: virtually every trader will come into and go out of the market **without** making or taking delivery of the deliverable.

[7] Another of the many differences between stock and commodity futures trading is that the commodity exchange publishes the amount of the open interest, that is, the amount of un-liquidated contracts that are open each day. S.Appx.82,103-4. This open interest generally increases until approximately twenty days before deliveries are scheduled to begin. *Id.* Then traders generally cease to make new trades in the soon-to-expire futures contract and the open interest decreases to virtually zero. *Id.*

uneconomic conduct, including demanding all-time record deliveries, caused all-time record price ***di***vergence between the futures and cash prices. S.Appx.144-45, 207.

Defendants' uneconomic conduct and manipulation began on May 9, 2005, which was twenty-two days before the start of deliveries in the June Contract and at the time that new traders were no longer entering the June Contract and its open interest began to decline.

F. Defendants Conceded At Oral Argument Below That The Class Is Properly Certified To The Extent of The $1.83 Trillion In Short Positions Sold Prior To May 9

In the Seventh Circuit, Defendants conceded at oral argument that certification of persons who opened the short positions prior to May 9, 2005 was proper. See Transcript of Oral Argument at 6-7, *Kohen v. Pacific Investment Management Company LLC*, No. 08-1075, 2009 WL 925914 (7th Cir., April 1, 2009).

The amount of June Contracts open on May 9 was $1.83 trillion. S.Appx. 103-104. As the shorts bought back their contracts, the open interest declined to $18.6 billion by June 14 and $15.1 billion by the end of all trading on June 21, 2005. *Id.* Defendants conceded that the $1.83 trillion in short positions established prior to the Class Period by selling at zero artificiality,

and who made their liquidating purchases at allegedly artificial prices, are properly certified.[8]

G. Defendants Objected To The Inclusion In The Class Of The Very Persons Who, Contrary to Market Norms, Made New Sales of June Contracts After May 9 And Thereby Retarded The Degree of Artificially High Prices Caused By The Manipulation

At oral argument in the Seventh Circuit, Defendants continued to object to the inclusion in the class members who initiated their short position on and after May 9, 2005 --- when Defendants' manipulation began. Those persons allegedly received some price artificiality on their sale transaction.[9]

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[8] Applying the amount of price artificiality that Defendants caused to the minimum net liquidation each day (that is, to the decline in the reported open interest), Plaintiffs' expert calculated a "top down" conservative minimum of $632,000,000 in aggregate damages. Appendices to Defendants' Motion To Strike, *Kohen v. Pacific Investment Management Co. LLC.*, No. 05 C 4691 (N.D.Ill., filed Jun. 12, 2007) [Docket No. 277] at Ex. B ¶2. This conservative estimate is substantially less than Defendants' one **billion dollar profit** on their positions. Docket No. 126 at p. 9. It is a fraction of the aggregate damages that would be produced by using overall trading volume.

[9] The CEA does not define "actual damages" in Section 22(a). *U.S. Commodity Futures Trading Commission v. Enron Corp. and Hunter Shively*, 2004 WL 594752, *4 (S.D. Tex. Mar. 10, 2004); *In re Cannon*, 230 B.R. 546, 594 (W.D.Tenn. 1999). The term has been flexibly and liberally construed to include unjust enrichment, *Randall v. Loftsgaarden*, 478 U.S. 647, 660 (1986) (securities), as well as to achieve the CEA's remedial purposes. *See Leist*, 638 F.2d at 304.

But the economic theory of self-correcting forces of the market posits that, contrary to the normal avoidance of the June Contract as declines in its open interest begins, at least some new shorts will enter the market in order to sell into the artificially high prices caused by manipulation.

1. Plaintiff Breakwater Trading LLC Lost $15,513,288 on Such New Sales

Although excessive reliance on the self-correcting forces of the market has been discredited,[10] these new shorts theoretically reduce the degree of "success" of the manipulation. They reduce the degree of price distortion signals sent by the manipulation to the public and thereby help the public.

Helping the public in this manner, Plaintiff Breakwater lost $15,513,288 on its sales of June Contracts. See Declaration of Jennifer Tan, *Kohen v. Pacific Investment Management Co. LLC.*, No. 05 C 4681 (N.D. Ill., filed Oct. 15, 2008) [Docket No. 422], Ex I.

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[10] House Committee on Oversight and Government Reform, hearing, October 23, 2008, testimony of Alan Greenspan: "I made a mistake in presuming that the self-interest of organizations, specifically banks and others, were such that they were best capable of protecting their own shareholders and their equity in the firms.

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Mr. Greenspan: "Precisely. That's precisely the reason I was shocked...."

Transcript at pp. 33-34, 37 available at http://oversight.house.gov/images/stories/documents/20081024163819.pdf

H. Defendants Concede That All of These Class Members Have Constitutional Injury And Standing

In this Court, Defendants conceded that all Class members have Constitutional injury and standing. Pet.7.

I. Plaintiffs' Uncontested Showing That The Certified Class Was Extremely Homogeneous And Much Smaller Than Previously Certified CEA Manipulation Classes

On their motion for class certification, Plaintiffs submitted the affirmations and reply affirmations of Craig Essenmacher, Esq. and Professor Christopher L. Gilbert as well as an Affidavit of Thomas Rubio. Docket Nos. 64, 65, and 418. Plaintiffs demonstrated that the proposed class herein is much smaller and more homogenous than the (admittedly rare) classes on which CEA manipulation claims had been unanimously certified for the prior twelve years. Docket No. 87 at pp. 1-2; *see* Matrix and Argument "C" *infra* (describing Plaintiffs' uncontested showing and cases).

J. Defendants Successfully Achieved An Early Cut-Off To Discovery, Failed To Contest The Adequacy of Class Counsel, And Submitted Plaintiffs' Merits Liability And Damages Expert Report In A Surreply On The Class Motion

Before the class motion was decided, all discovery was completed, and the parties' merits and rebuttal merits experts reports had been exchanged.

Defendants submitted portions of one of Plaintiffs' merits expert report by Professor Craig Pirrong ("Pirrong Report") (and no rebuttal or Defendants' merits expert report) in Defendants' Surreply on the class motion. Def. Sur-Reply in Opp. To Motion for Class Cert., *Kohen v. Pacific Investment Management Co. LLC.*, No. 05 c 4681 (N.D.Ill., filed Mar. 28, 2007) [Docket No. 260] at 2-3.

The Pirrong Report contained extensive fact and opinion evidence that Defendants had committed multiple manipulative acts (S.Appx.144-5); and that these acts had caused June Contract prices to be artificially high. S.Appx.145.

On the class motion, Defendants failed to dispute various issues, including the adequacy of class counsel requirement of Rule 23(a)(4). *Kohen v. PIMCO*, 244 F.R.D. 469, 479 (N.D. Ill. 2007) ("Defendants have failed to dispute adequacy of counsel, and the Court is satisfied that plaintiffs' counsel will vigorously

prosecute this case").[11] In contrast, in *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 625-28 (1997), the class counsel were found not to be adequate.

Defendants did not request a hearing on the class motion. *See* Defendants' Opposition to Class Certification and sur-reply to Class Certification, *passim*.

K. The District Court Expressly Found That Plaintiffs Had Proved Each Requirement of Rule 23

On July 31, 2007, the District Court certified a class as follows: All persons who purchased, between May 9, 2005 and June 30, 2005 ("Class Period"), inclusive, a June 2005 10-year Treasury note futures contract in order to liquidate a short position (the "Class"). Pet.App.24a.

Citing to *Szabo v. Bridgeport Machs., Inc.*, 249 F.3d 672, 676 (7th Cir. 2001) and applying *Szabo*'s requirement that Plaintiffs must prove each element of Rule 23, the District Court specifically considered each element and specifically found that Plaintiffs had proved each requirement of FRCP Rule 23(a) and 23(b)(3). Pet.App.27a-39a.

The District Court also carefully considered each of Defendants' arguments and rejected as inapplicable to

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[11] *Compare* Plaintiffs Class Cert. Reply Br. at p. 23 (asserting that Petitioners failed to dispute Plaintiffs had established this aspect of Rule 23(a)(4)) *with* PIMCO Surreply, *passim* (failing to contest same).

the facts many of the legal precedents still offered by Defendants. Pet.App.24a-25a, 34a, 37a n. 4. Expressly addressing Defendants' argument that the defined class may include "uninjured members," Pet.App.25a, the District Court correctly determined that all class members suffered injury when they covered their short positions at artificially inflated prices. The District Court exercised its discretion to find that any netting calculations of the extent (not fact) of injury should more efficiently be managed and resolved when damages are normally proved. Pet.App.25a-26a. ("defendants' concerns over the final determination of net damages for some individual members of the class should be resolved in the damages stage of the litigation").[12]

L. After Defendants Conceded At Oral Argument That Most Of The Class Should Be Certified, The Seventh Circuit Unanimously Refused To Modify The Class

Defendants obtained interlocutory review under Rule 23(f) and conceded at oral argument of their appeal that at least a class of persons who sold short prior to May 9, 2005 was appropriate here. See Transcript, 2009 WL 925914 at pp. 6-7. After considering all of Defendants' arguments, the Court of Appeals refused to modify the class definition and unanimously affirmed the District Court. *See infra*

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[12] Defendants' own cases recognize the firmly established principle that district courts are granted a wide range of discretion in resolving manageability concerns because of their greater familiarity and expertise with factual matters in particular cases. *Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 259 F.3d 154, 191 (3d Cir.2001) (collecting cases).

(correcting Defendants' misinterpretations of Decision). Defendants' petition for rehearing *en banc* was denied without dissent. Pet.App.52a-53a.

Defendants now seek further interlocutory review before this Court to modify the scope of the class definition contained in the inherently conditional interlocutory class certification order. Rule 23(c)(1)(C) (expressly providing that such certification "may be altered or amended before final judgment").

ARGUMENT

A. Not Only Is There No Conflict But This Court Would Be The First To Hold That Section 22(A) Of The CEA Requires Proof Of Actual Damages As A Prerequisite To Statutory Standing

Defendants' premise that there are "uninjured" members in the class is clearly wrong. See Reasons For Denying Certiorari *supra*.

Defendants ask this Court to become the first ever to hold (a) that "actual damages" is an element of a claim under Section 22(a) of the CEA rather than merely a limitation on the types of damages (b) notwithstanding Defendants' repeated arguments that "injury" and standing are different, Pet.16, if a Plaintiff fails to prove a supposed element of a claim at trial, then this retroactively means that the Plaintiff did not have statutory injury and standing from the outset, Pet.9a-10a, and/or (c) that "actual damages" is an element which, if not pled, deprives a plaintiff of the injury required for CEA statutory standing.

Defendants argue that, if this Court holds all the foregoing, then certain class members will (notwithstanding their conceded Constitutional injury) be "uninjured" class members, and the Decision will conflict with the precedent of this Court and the Rules Enabling Act by including those uninjured members in the Class. But the CEA is remedial legislation and the term "actual damages" has been flexibly construed and not necessarily equated with net damages.

Defendants cite cases under Section 22(a) that do not begin to suggest that the Court should become the first ever to make the foregoing holdings. Pet.15-17.[13]

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[13] Defendants' cases uniformly hold, without reference to the pleading of actual damages, that the only persons subject to a private right of action under Section 22(a)(1) are those involved in the disjunctive categories of transactions described in Section 22(a)(1). See:

- *Kolbeck v. LIT America, Inc.*, 923 F.Supp. 557, 566 (S.D.N.Y. 1996) (Mukasey, J.) (dismissing CEA fraud claims without mentioning "actual damages" but because the complaint pleaded "none of the listed relationships" in subparagraphs (A)-(D) with the defendants);
- *Damato v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 878 F.Supp. 1156, 1161 (N.D.Ill. 1995) (dismissing certain defendants because "the only persons subject to a private right of action under §22(a)(1)(C)(iii) of the CEA are the persons who sold or took orders for interests in the commodity pool"), *aff'd sub nom. Damato v. Hermanson*, 153 F.3d 464, 470 (7th Cir. 1998) (§ 22(a)(1) limits recoveries to actual damages resulting from one or more of the transactions referred to in subparagraphs (A) through (D)); and
- *Three Crown Ltd. P'ship v. Caxton Corp.*, 817 F.Supp. 1033, 1043 (S.D.N.Y. 1993) ("22(a)(1) lays out what are in essence 'conditions precedent' which must be alleged in addition to the elements required to plead a

A further reason to deny certiorari is that Defendants' citation to *Warth v. Seldin*, 422 U.S. 490 (1975), introduced by a "*see*" signal, Pet.16, contradicts Defendants' arguments. Although *Warth* did not discuss "actual damages," *Warth* did hold a plaintiff may not assert merely a "**generalized grievance**" or the rights of third parties, and described "the standing question . . . [as] whether the constitutional or statutory provision on which the claim rests properly can be understood as granting persons in the plaintiff's position a right to judicial relief." *Warth,* 422 U.S. at 500 (footnote omitted).

Compare, Steel Co. v. Citizens for a Better Environment, 523 U.S. 83, 94 n.2, 97 (1998) (statutory standing "has nothing to do with whether there is a case or controversy under Article III," *i.e.*, a demonstration of "injury-in-fact" and "effectiveness of the requested remedy," but whether the plaintiff "has a cause of action under the statute") *with Transnor (Bermuda) Ltd. v. BP North America Petroleum*, 736 F.Supp. 511, 522-23, n.15 (S.D.N.Y. 1990) (legislative history of Section 22 of the CEA shows that "actual damages" provision was intended "to limit a plaintiff's recovery to damages to assets which are traded" on the futures market).

Clearly, short sellers who pay the artificially high price caused by a "short squeeze" manipulation are not

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violation of one of the substantive violations of the CEA;" although plaintiffs had pleaded actual damage to their futures positions, their CEA claims were dismissed because "plaintiffs' theory of manipulation is not one for which there is a private right of action under §22(a)(1)(D)").

asserting "generalized grievances". Rather, they are complaining of, and were allegedly injured by the evil of price manipulation (*i.e.*, the artificial prices) that Congress has been trying to prevent for almost ninety years. See *Leist*, 638 F.2d at 328, 335-7.

Certiorari should be denied. But if there were any review of the Decision, this Court would agree with the Decision and find that all Class members clearly have statutory standing and "injury" under the CEA.

B. Certain of Defendants' Supposedly Conflicting Cases Expressly Recognize That The Class Certification Result Would Have Been Different In The Very Different Type of Claim Here

Based on their faulty "uninjured class member" premise, Defendants assert that a conflict exists between (a) how the Decision applied the "adequacy" or "predominance" requirements of Rule 23(a)(4) and Rule 23(b)(3) to the specific CEA manipulation claim and the final merits expert report here, and (b) how decisions in the other Circuits have applied such requirements to the very different claims and circumstances present there. Pet.12-15.

But there is no conflict. First, Defendants' premise fails because, unlike in Defendants' cases, all Class members here (a) were injured, (b) were injured in the exact same standardized contract in the exact same way, (c) were subject to the exact same rule set and violation, and (d) were actually proved, by the final merits expert report, to have been injured. Only the issue of the amount of damages remained.

Thus, very unlike the differing rule-sets or differing contracts or treatments which class members experienced and the very different violations present in Defendants' cases (Pet.12-15), Plaintiffs here made an **undisputed** demonstration that:

1. Each Class member purchased the exact same standardized, fungible and interchangeable June Contract during the period in which prices were alleged to be unlawfully high. Plaintiffs' First Amended Motion For Class Certification, *Kohen v. Pacific Investment Management, Co. LLC*, No 05 C 4681 (N.D.Ill., filed Jul. 5, 2006) [Docket No. 67] at pp. 1-2.

2. Each Class member did so in the exact same centralized CBOT market place subject to the exact same standardized customs, practices, and binding CBOT rules. *Id.*

3. The price that each Class member paid allegedly was unlawfully inflated by Defendants' exact same highly unusual departure from their prior history of conduct. *Id.*

4. Each Class member made the exact same legal claim with the exact same elements: Defendants manipulated upward the prices of the June Contract in violation of the CEA. *Id.*

5. The amount of unlawful price artificiality (the so-called "price ribbon") paid by each Class member would be (and was) established by the same common, class-wide econometric proof.

6. This common class-wide econometric formula was based upon the exact same corpus of objective historical facts. This included, for example, the exact same long history of (a) prices, open interest, volume of futures trading, (b) the pricing relationships between the June Contract and other instruments and, (c) the positions purchased or sold, the deliveries taken, and other conduct by Defendants. S.Appx.27-30.

7. Any artificiality received on any sales transaction by Class members during the Class Period could be netted against their artificiality paid—all as calculated by applying the price ribbon to the record of each Class member's specific trades (but **not** to the average artificiality for the day, as Defendants now misstate). M.Decl., Ex. 21 at pp. 50-52. (Plaintiffs specifically dispute that they or any Class members mentioned by Defendant are "net gainers".)

Consistent with the foregoing decisive factual differences between this CEA manipulation claim and the very different claims and circumstances in the cases Defendants cite, Defendants' own cases expressly recognized that the class certification results they were reaching would have been different if the claim were an open market manipulation case. *Compare Langbecker v. Electronic Data Systems Corp.*, 476 F.3d 299, 315 (5th Cir. 2007) (claims were not the uniform effort to prove misrepresentations about securities but efforts to "second guess" years of fiduciary judgments involving a multitude of considerations) *with Newton*, 259 F.3d at 188-89 (alleged fraud was not "on the market" but only on those class members whose trades could have been executed at better prices).

1. Given The Non-Standardized Contracts Held By The Class Members In *Valley Drug*, The One Sentence In That Opinion Does Not Represent A Conflict, Let Alone An Important Conflict On The Same Matter

Defendants try to overcome the foregoing harmony between their own cases and the Decision by focusing on one sentence from *Valley Drug Co. v. Geneva Pharmaceuticals, Inc.*, 350 F.3d 1181, 1190 (11th Cir. 2003). There, three wholesalers (representing over 50% of the class) had unique cost-plus sales contracts that made the alleged violation beneficial to them under their unique contracts. Pet.12.

In this very different fact context, one sentence in *Valley Drug* stated that "net gainers" should not be included in the class. *Valley Drug*, 350 F.3d at 1190.

There is no conflict "on the same important matter" informing this Court's discretion to grant the petition. Supreme Court Rule 10(a).

Moreover, there is not even a lesser conflict between the Decision and *Valley Drug*'s one sentence dictum. Rather, the Seventh Circuit pragmatically reasoned as follows. While some cases contain language to the effect that "it must be reasonably clear at the outset that all class members were injured by the defendant's conduct," such cases "focus on the class definition; if the definition is so broad that it sweeps within it persons who could not have been injured by the defendant's conduct, it is too broad." *Compare*, Pet.App.10a-11a with Pet.12-13.

Again, here, all Class members purchased the same, standardized contract and all could have been (and were proved to have been) injured. But in *Valley Drug*, the wholesalers had very different, cost-plus contracts such that defendants' own records showed that more than 50% of the defined class members, from the outset of the litigation, were benefiting from the alleged violation that the private suit sought to stop. *Valley Drug*, 350 F.3d at 1190.

Defendants' other cases are even more distinguishable:

- *Phillips v. E.T. Klassen*, 502 F.2d 362 (D.C.Cir.), *cert. denied*, 419 U.S. 996 (1974) (representative plaintiffs were postal employees who had been offered retirement packages but the likelihood was that many Class members were "pleased" and would want neither to return to their former jobs nor refund their benefits. *Id* at 369. "The issue of defining the class, and its proper representation, may arise in some measure in all class actions, but it is not likely to cut as keenly when only future relief is sought. . . ." *Id.* at 368.)

- *Pickett v. Iowa Beef Processors*, 209 F.3d 1276, 1277-1280 (11th Cir. 2000) (discriminatory treatment (not price manipulation, as Defendants misstate) claim under the Packers and Stockyards Act, 7 U.S.C. §§ 181 *et seq.*, that included in the class the persons who allegedly were discriminated in favor of; *Id.* at 1280);

- *Allied Orthopedic Appliances, Inc. v. Tyco Healthcare Group L.P.*, 247 F.R.D. 156, 166-69,

177 n. 2 (C.D.Cal. 2007) (class definition included large hospitals, who had sufficient market power to obtain favorable pricing without the challenged discounts, and small hospitals who relied upon such discounts);

- *Langbecker*, 476 F.3d at 304, 314-16 (ERISA claims charging breach of fiduciary duties for offering company stock as a plan investment and seeking damages and injunctive relief, 476 F.3d at 304, but tens of thousands of class member-plan participants maintained their investments in the challenged stock after the disclosures, undermining the claim);

- *In re Hydrogen Peroxide Antitrust Litig.*, 552 F.3d 305 (3d Cir. 2009) (multiple non-standardized products sold by different producers in different markets over a twelve year period with divergent pricing patterns)

- *Newton*, 259 F.3d 154 (alleged breach of duty of best execution, had to be examined on a trade-by-trade basis in order to see if the execution was not the best);

- *Bell Atlantic Corp. v. AT&T Corp.*, 339 F.3d 294 (5th Cir. 2003) (non-market trading case which required estimates of the value to each class member of withheld caller I.D. information).

C. Defendants Fail To Manufacture A Conflict Among The Circuits On The Inquiry Demanded Prior To Certifying A Class

After more than ten years' experience with Rule 23(f), the circuits are strongly aligned in requiring more, not less, "rigor" in certifying classes. *Contrast*, Pet.17-22, citing *General Telephone Co. of the Southwest v. Falcon*, 457 U.S. 147, 161 (1982). Defendants misstate several decisions and ignore scholarship demonstrating the uniform "rigorous analysis" performed by the circuits.[14]

Brown v. American Honda (*In re New Motor Vehicles Canadian Export Antitrust Litig.*), 522 F.3d 6 (1st Cir. 2008) found, not conflict, but that "[o]ur sister circuits agree that when class criteria and merits overlap, the district court must conduct a searching inquiry regarding the Rule 23 criteria". *Id.* at 24. The First Circuit did not reach the issue of whether findings were necessary and thus raised no conflict, holding instead that in this specific instance, plaintiffs' "novel and complex" theory as to injury affecting

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[14] Two authors who regularly represent defendants found "near unanimity." William Kolasky and Kevin Stemp, *Antitrust Class Actions: More Rigor, Fewer Shortcuts*, CLASS ACTION REPORTS, Vol. 30 No. 6, at 3 (Thomson Reuters Nov.-Dec. 2009) available at http://www.wilmerhale.com/files/Publication/da664923-f9dd-4b75-bd1e-f43f8806d246/Presentation/PublicationAttachment/140b9324-0138-4f0a-b8f4-f9d108e1ce15/Kolasky_AuthorArticle.pdf. "The courts of appeals have ... moved to inject much greater rigor into the class certification process." *Id.* at 2. Since 2005, nearly two-thirds of Rule 23(f) appeals have been from denials, giving rise to a "reasonable hypothesis" that district courts are denying certification in a higher percentage of cases due to the increased rigor required by the courts of appeals. *Id.* at 6-7, Tables 2&3.

potentially millions of negotiated vehicle purchases required a "searching inquiry" into the viability of the theory and the completion of class discovery.

Miles v. Merrill Lynch & Co., (*In re Initial Public Offering Sec. Litig.*), 471 F.3d 24 (2d Cir. 2006) and *In re Hydrogen Peroxide Antitrust Litig.*, 552 F.3d 305, 320 (3d Cir. 2009) are also unavailing. *In re IPO*, rather than illustrating that the lower courts are "perplexed" by the Rule 23 standards, Pet.18 n.4, took pains to note that in requiring district courts to make a "definitive assessment of Rule 23 requirements, notwithstanding their overlap with merits issues," the Second Circuit was aligned with the "strong line of authority" of seven other circuits. *IPO*, 471 F.3d at 38-39, citing *In re PolyMedica Corp. Securities Litigation*, 432 F.3d 1 (1st Cir. 2005); *Unger v. Amedisys, Inc.*, 401 F.3d 316, 319 (5th Cir. 2005); *Blades v. Monsanto Co.*, 400 F.3d 562, 575 (8th Cir. 2005); *Gariety v. Grant Thornton, LLP*, 368 F.3d 356 (4th Cir. 2004); *Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 259 F.3d 154, 166 (3d Cir. 2001); *Szabo v. Bridgeport Machines, Inc.*, 249 F.3d 672 (7th Cir. 2001); and *Love v. Turlington*, 733 F.2d 1562, 1564 (11th Cir. 1984).

Hydrogen Peroxide similarly required an examination of the factual record underlying the certification decision, the court noting its agreement with the decisions of seven other circuits. *Hydrogen Peroxide*, 552 F.3d at 316-20.

Finally, *Loftin v. Bande (In re Flag Telecom Holdings Ltd. Sec. Litig.)*, 574 F.3d 29 (2d Cir. 2009), contrasts the Fifth Circuit's approach on certification of Rule 10b-5 claims in *Oscar Private Equity Inv. v. Allegiance Telecom, Inc.*, 487 F.3d 261 (5th Cir. 2007)

with that of securities decisions in the Southern District of New York. But because the triggering of the fraud-on-the-market presumption---a substantive securities law requirement also not present in CEA manipulation cases---was **not** in issue, the Second Circuit had no need to reach it. Therefore, *Flag Telecom* exposes no conflict with *Oscar* in Rule 23 procedure (or even in how to handle securities law class actions). *Flag Telecom*, 574 F.3d at 39-40. Thus, there particularly is no conflict that can be addressed by review of this CEA manipulation class action.

D. It Is The Defendants' Discredited Argument, Not The Decision, That Conflicts With Other Circuit Courts Concerning The Application Of The Rule 23(a)(4) "Adequacy" Requirement To Classes That Include Persons Who Both Bought And Sold

1. Market Trading Cases

There is no conflict between the Decision and the decisions of this Court or other Circuit courts concerning the "adequacy" requirements of FRCP Rule 23(a)(4) in open market trading classes that include persons who both bought and sold. *Compare,* Pet.21-30. Indeed, Defendants **fail** to cite to **any** Circuit court decisions refusing to certify a CEA manipulation class action or even a securities fraud class action on the grounds of FRCP 23(a)(4) adequacy because certain members of the class both purchased and sold. Pet. *passim*.

In fact, the Decision is consistent with the other Circuit court decisions and almost all other decisions

in certifying classes of persons who both bought and sold. Lacking any conflict among the Circuits, Defendants' primary support for their proposed move in the wrong direction is *In re Seagate Technology II Sec. Litig.*, 843 F.Supp. 1341, 1359 (N.D.Cal. 1994). Although a class had been certified in *Seagate* some three years earlier, the *Seagate* District Court nonetheless mused that there might be various forms of potential class member conflict, including a potential "seller-purchaser" conflict in "shaping the evidence." *Id.*, at 1359, 1361; Pet., *passim*.

The *Seagate* Court acknowledged that courts had consistently rejected arguments that volatility in the amount of artificial price inflation at different points in the class period defeated adequacy or class certification. *Id.* at 1358-59. *Seagate* did not decertify the class, but resolved to conduct an evidentiary hearing (which, in fact, was never held). *Id.* at 1367.

The musings of *Seagate* contravene controlling Ninth Circuit law and have been repeatedly and almost unanimously "discredited." *See, e.g., In re Oxford Health Plans, Inc. Sec. Litig.*, 191 F.R.D. 369, 377 (S.D.N.Y. 2000). *Accord, e.g., Conn. Retirement Plans & Trust Funds v. Amgen, Inc.*, No. CV-07-2536, 2009 WL 2633743 at *6-7& n.9 (C.D.Cal. Aug. 12, 2009) (collecting cases); *In re Scientific-Atlanta, Inc. Sec. Litig.*, 571 F.Supp.2d 1315, 1334-35 (N.D.Ga. 2007) (collecting cases); *Freeland v. Iridium World Commn'ns Ltd.*, 233 F.R.D. 40, 49& n.11 (D.D.C. 2006) (collecting cases); *In re Daimler Chrysler AG Sec. Litig.*, 216 F.R.D. 291, 297& n.3 (D.Del. 2003) (collecting cases); *In re Gaming Lottery Sec. Litig.*, 58 F.Supp.2d 62, 70 (S.D.N.Y. 1999) (collecting cases).

Seagate itself recognized holes in its logic.[15] Although *Seagate* did not act on its discredited logic, Defendants cite to one district court decision which, in the sixteen years since *Seagate*, arguably did, by limiting the scope of class certification.[16] But neither this case nor Defendants' mis-cited other ones create an important conflict with the Decision.

Specifically, Defendants cite to dicta in *Ballan v. Upjohn Co.*, 159 F.R.D. 473, 485 (W.D.Mich. 1994)("the court need not adopt *Seagate II* in order to find Mr. Acito is an inadequate plaintiff, because Mr. Acito fails to satisfy the adequacy test under more conventional measures." As the sole representative, plaintiff was subjectively disinterested in and uninformed about the case, and plaintiffs' counsel had not performed adequately).

Incorrectly, Defendants claim support for *Seagate* from *Ziemack v. Centel Corp.*, 163 F.R.D. 530, 542-43 (N.D. Ill. 1995) (citing *Ballan*, but holding that it was premature to suggest that in-out stock traders would lack standing; denied motion to decertify pending joint

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[15] For example, *Seagate*, 843 F.Supp. at 1359-60, acknowledged *In re LTV Sec. Litig.*, 88 F.R.D. 134 (N.D.Tex. 1980): "We do not find such a potential conflict to be sufficient to deny class certification. Significantly, available techniques of proof such as econometric modeling are sufficiently demanding of internal consistency as to reduce the opportunity for such manipulation of data." *Id.* at 149.

[16] That case was *In re Physician Corp. of America Sec. Litig.*, No. 97-3678-CIV, 2003 WL 25820056 at *9-10 (S.D. Fla. May 21, 2003)(narrowing class definition where purchasers who retained stock after curative disclosures argued that disclosures were inadequate, creating issue as to proof of violation with class members who sold after disclosures).

status report on theories of liability, potential adverse interests of in-out plaintiffs, and sub-classing).

Other cases in which Defendants assert that the courts implicitly adopted Seagate's reasoning *sub silentio,* simply did not do so.[17]

In reality, it is the Defendants' position that is in conflict with the other courts. That is, at precisely the time when more deterrence of wrongdoing is needed in the futures and other financial markets, Defendants seek to hasten the rapid declines in deterrence by asking this Court to advance an argument that has been repeatedly rejected for thirty-plus years.

Moreover, CEA manipulation cases far longer and more complex than this one have found no problems with adequacy, and repeatedly certified classes in both the District and the Circuit courts.

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[17] One CEA manipulation case, *Premium Plus Partners, L.P. v. Davis*, No. 04 C 1851, 2008 WL 3978340 (N.D.Ill. Aug. 22, 2008), suffered from an abnormally defined class that included persons who traded for an indeterminate, long period after the alleged manipulation had ended. This created the type of unidentified or future class member problem that was even more present in *Amchem Prods. v. Windsor*, 521 U.S. 591 (1997).

Although the District Court initially denied certification of far larger classes in the *Centurions v. Ferruzzi Trading Int'l*, No. 89 C 7009, 1994 WL 114860 (N.D.Ill. Jan. 7, 1993), and *McCullough v. Ferruzzi Trading Int'l*, No. 90 C 1138, 1993 WL 795256 (N.D.Ill. 1993) decisions cited by Defendants, the same Court later in the same case, did certify a smaller class. *In re Soybean Futures Litig.*, No. 89 C 7009, 1993 U.S.Dist. LEXIS 18738 at *33 (N.D.Ill. Jan. 11, 1994)).

The instant class is much smaller and less diverse than even the certified class in *Soybean Futures*. *See* Matrix.

Case Name	Time Period	No. of Futures Contracts	Class Members	Type of Manipulation
Plaintiffs' Proposed Class Here	31 trading days	1	Short futures traders	Exclusively Upward
In re Natural Gas Commodities Litig., 231 F.R.D. 171, 179 (S.D.N.Y. 2005), ***petition for review denied*** August 1, 2006 ("*In re Natural Gas*")	3 year class period	60	Short and Long futures traders	Upward and Downward
In re Sumitomo Copper Litig., 182 F.R.D. 85, 87 (S.D.N.Y. 1998) ("*Sumitomo III*")	2 year class period	36	Short and Long futures traders	Rolling
In re Sumitomo Copper Litig., 194 F.R.D. 480 (S.D.N.Y.	2 and a half year class period	30	Short and Long futures traders	Rolling

2000), ***appeal denied***, 262 F.3d 134 (2d Cir. 2001) ("*Sumitomo II*")				
In re Soybean Futures Litig., No. 89 C 7009 (N.D. Ill. Dec. 27, 1993) ("*Soybeans*")	41 trading days	2	Short and Long futures traders	Exclusively Upward

2. Inapposite Cases

Defendants also cite to non-CEA, non-open-market-trading cases which, rather than presenting any conflict regarding the requirements of Rule 23(a)(4), apply the requirements of Rule 23(a)(4) to radically different facts. Pet.22-25. In *Amchem Prods. v. Windsor*, 521 U.S. 591 (1997), this Court, noting that "[n]o settlement class called to our attention is as sprawling as this one," found a profound diversity of interests among manifestly-injured and exposure-only asbestos plaintiffs.

East Texas Motor Freight System, Inc. v. Rodriguez, 431 U.S. 395 (1977) involved a trial dismissing plaintiffs' individual discrimination claims and the *sua sponte* certification on appeal of a class to be represented by those plaintiffs. This Court held that, having lost at trial, plaintiffs were ineligible to

represent a class of injured plaintiffs, and noted that "[o]bviously, **a different case** would be presented if the District Court had certified a class and only later had it appeared that the named plaintiffs were not class members or were otherwise inappropriate class representatives." *Id.* at 406 n. 12 (citations omitted).

Valley Drug, 350 F.3d 118, emphasized that it was only the specific nature of the product (drugs experiencing inelastic demand) and the differing types of contracts (three national wholesalers with over 50% of the claims had cost-plus contracts that experienced unchallenged benefit from maintaining the status quo) that enabled it to conclude that a fundamental conflict existed under 23(a)(4). *Id.* at 1191.

E. More Deterrence Of CEA Manipulations, Not Less, Is Now Needed, And The Petition Involves No Issue Of Public Importance

Incorrect facts make bad policy. Defendants cherry-pick dated information to make empirical assertions about potential **securities** class action abuses. Pet.30-32.

First, there are no abuses in, and have never been any abuses in, CEA manipulation class actions. *Compare* Private Securities Litigation Reform Act, 15 U.S.C. §78u-4(b)(2) (finding abuses in securities class actions and imposing heightened pleading standards in securities cases) *with* CEA, 7 U.S.C. §1 *et seq.* (no finding of any abuses in class actions under the CEA).

Commodity futures manipulation class actions are exceedingly rare. A WESTLAW search for commodity manipulation class actions yielded only 32 entries,

going back to 1974.[18] When duplicate entries and non-commodity cases were culled from the list, only 14 cases remained, averaging fewer than one commodity manipulation class action filed every 2½ years.

After the implosion of the financial system and repeated "bubbles" in energy and other commodity futures prices, more deterrence from private lawsuits and regulation—not less—is needed. *Compare, Cange*, 826 F.2d at 584 (private actions are of "critical importance" to enforcement of CEA) *with* J. Blas and C. Flood, *Prices Were Hit By Asset Bubble, Says CFTC Head*, FINANCIAL TIMES, June 2, 2009, and C. Rampell, *Lax Oversight Caused Crisis, Bernanke Says*, THE NEW YORK TIMES, Jan. 4, 2010, p. 1 Col. 4.

Defendants do refer to thirty-year-old assertions of "blackmail settlements" in class actions generally. But the author, Judge Henry Friendly, separately emphasized the policy need for private suits against "big manipulators" in a case involving class actions in the commodity futures markets. *Leist*, 683 F.2d at 305.

Courts and commentators have long rejected the "blackmail settlements" charge against class actions. *E.g.*, Allan Kanner & Tibor Nagy, *Exploding The Blackmail Myth: A New Perspective On Class Action Settlements*, 57 BAYLOR L.REV. 681, 693-95 (2005) ("blackmail" concerns are unsupported either at law or

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[18] The search of the ALLFEDS database specified the following terms: "class /3 action /p commodit! /s manip!" The 32 entries included multiple decisions involving the same case in the district courts, the courts of appeal, and this Court, as well as non-commodity cases in which the search terms appeared.

by empirical evidence, and "hydraulic pressure on defendants to settle" is "itself more myth than reality," as dispositive motions and interlocutory appeals provide important legal safeguards against meritless class actions).

Defendants also cite *In re Rhone-Poulenc Rorer, Inc.*, 51 F.3d 1293, 1298-99 (7th Cir.), *cert. denied*, 516 U.S. 867 (1995), but that Court expressly added that "[w]e do not want to be misunderstood as saying that class actions are bad because they place pressure on defendants to settle."

Indeed, to achieve their deterrence benefits, class actions must impart some pressure when the merits of the case are strong. Defendants have conceded in the Court below that a substantial class is proper here. 2009 WL 925914 at pp. 6-7. Therefore, the extensive merits record of Defendants' all-time record uneconomic conduct, and the resulting all-time record prices, is the only matter of importance to settlement, trial, deterrence, justice or "pressure."

Because they are wholly inapposite to this CEA manipulation class action, Defendants' empirical assertions about securities class actions would argue at most only for granting certiorari in a securities law case.

But Defendants' dated empirical assertions convey a misleading picture about even securities class actions. Defendants ignore the Cornerstone Research mid-year 2009 report, which showed a "pronounced drop off" of 22.3% in securities class action filings in the first half of 2009 compared to the first half of

2008,[19] and Cornerstone's 2009 year-end report confirmed that securities filings were down 24% from 2008.[20]

Although Defendants assert that securities class actions involve increasingly large settlements, their own sources show more than a 50% decline in average securities class action settlements in 2008. Pet.31 (citing Ellen M. Ryan & Laura E. Simmons, Cornerstone Research, *Securities Class Action Settlements, 2008 Review and Analysis* 2, *available at* http://securities.stanford.edu/Settlements/REVIEW_1995-2008/Settlements_Through_ 12_2008.pdf.

Finally, suppose Defendants' empirical or other assertions had established a problem with the far more numerous federal securities or antitrust law class actions. The main issues in those class actions would not be addressed by granting certiorari here because this case does not involve (a) the fraud on the market, efficient market and loss causation issues that dominate securities class motion practice (pp. 29-30 *supra*), or (b) the suitability of plaintiffs' proposed impact model, issues that dominate antitrust class motions (where different products are sold in multiple

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[19] Cornerstone Research, *Securities Class Action Filings: 2009 Mid-Year Assessment* 2 (2009), available at http://securities.stanford.edu/clearinghouse_research/2009_YIR/Cornerstone_ Research_Filings_2009_MidYear_Assessment.pdf.

[20] Cornerstone Research, *Securities Class Action Filings, 2009: A Year in Review* 2 (2009), *available at* http://securities.stanford.edu/clearinghouse_research/2009_YIR/Cornerstone_ Research_Filings_2009_YIR.pdf.

locales pursuant to different contracts with different price profiles (pp. 25-27 *supra*)).[21]

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

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[21] Pursuant to Supreme Court Rule 15.2, Plaintiffs dispute as incorrect Defendants' (mis)statements that Plaintiffs' expert reports supposedly are in conflict (see 2009 WL 925914 at *11), or supposedly reveal certain patterns of price artificiality, and that class members supposedly traded in certain patterns. Pet.23,26.

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APPENDIX A

United States Code Annotated
Title 7. Agriculture
Chapter 1. Commodity Exchanges

7 U.S.C. §25

§ 25. Private rights of action

(a) Actual damages; actionable transactions; exclusive remedy

(1) Any person (other than a registered entity or registered futures association) who violates this chapter or who willfully aids, abets, counsels, induces, or procures the commission of a violation of this chapter shall be liable for actual damages resulting from one or more of the transactions referred to in subparagraphs (A) through (D) of this paragraph and caused by such violation to any other person–

(A) who received trading advice from such person for a fee;

(B) who made through such person any contract of sale of any commodity for future delivery (or option on such contract or any commodity); or who deposited with or paid to such person money, securities, or property (or incurred debt in lieu thereof) in connection with any order to make such contract;

(C) who purchased from or sold to such person or placed through such person an order for the purchase or sale of–

(i) an option subject to section 6c of this title (other than an option purchased or sold on a registered entity or other board of trade);

(ii) a contract subject to section 23 of this title; or

(iii) an interest or participation in a commodity pool; or

(D) who purchased or sold a contract referred to in subparagraph (B) hereof if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract.

(2) Except as provided in subsection (b) of this section, the rights of action authorized by this subsection and by sections 7(d)(13), 7a-1(c)(2)(H), and 21(b)(10) of this title shall be the exclusive remedies under this chapter available to any person who sustains loss as a result of any alleged violation of this chapter. Nothing in this subsection shall limit or abridge the rights of the parties to agree in advance of a dispute upon any forum for resolving claims under this section, including arbitration.

(3) In any action arising from a violation in the execution of an order on the floor of a registered entity, the person referred to in paragraph (1) shall be liable for–

(A) actual damages proximately caused by such violation. If an award of actual damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under sections 2(a)(1) of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award; and

(B) where the violation is willful and intentional, punitive or exemplary damages equal to no more than two times the amount of such actual damages. If an award of punitive or exemplary damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under section 2(a)(1) of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award if the floor broker fails to do so, except that such requirement shall apply to the futures commission merchant only if it willfully and intentionally selected the floor broker with the intent to assist or facilitate the floor broker's violation.

(4) Contract enforcement between eligible counterparties

No agreement, contract, or transaction between eligible contract participants or persons reasonably believed to be eligible contract participants, and no hybrid instrument sold to any investor, shall be

void, voidable, or unenforceable, and no such party shall be entitled to rescind, or recover any payment made with respect to, such an agreement, contract, transaction, or instrument under this section or any other provision of Federal or State law, based solely on the failure of the agreement, contract, transaction, or instrument to comply with the terms or conditions of an exemption or exclusion from any provision of this chapter or regulations of the Commission.

(b) Liabilities of organizations and individuals; bad faith requirement; exclusive remedy

(1) (A) A registered entity that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by section 2(h)(7) of this title or sections 7 through 7a-2 of this title, (B) a licensed board of trade that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by the Commission, or (C) any registered entity that in enforcing any such bylaw, rule, regulation, or resolution violates this chapter or any Commission rule, regulation, or order, shall be liable for actual damages sustained by a person who engaged in any transaction on or subject to the rules of such registered entity to the extent of such person's actual losses that resulted from such transaction and were caused by such failure to enforce or enforcement of such bylaws, rules, regulations, or resolutions.

(2) A registered futures association that fails to enforce any bylaw or rule that is required under section 21 of this title or in enforcing any such bylaw or rule violates this chapter or any Commission rule, regulation, or order shall be liable for actual damages

sustained by a person that engaged in any transaction specified in subsection (a) of this section to the extent of such person's actual losses that resulted from such transaction and were caused by such failure to enforce or enforcement of such bylaw or rule.

(3) Any individual who, in the capacity as an officer, director, governor, committee member, or employee of registered entity [FN1] or a registered futures association willfully aids, abets, counsels, induces, or procures any failure by any such entity to enforce (or any violation of the chapter in enforcing) any bylaw, rule, regulation, or resolution referred to in paragraph (1) or (2) of this subsection, shall be liable for actual damages sustained by a person who engaged in any transaction specified in subsection (a) of this section on, or subject to the rules of, such registered entity or, in the case of an officer, director, governor, committee member, or employee of a registered futures association, any transaction specified in subsection (a) of this section, in either case to the extent of such person's actual losses that resulted from such transaction and were caused by such failure or violation.

(4) A person seeking to enforce liability under this section must establish that the registered entity [FN2] registered futures association, officer, director, governor, committee member, or employee acted in bad faith in failing to take action or in taking such action

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FN1 So in original. Probably should be "a registered entity".

FN2 So in original. A comma should probably appear.

as was taken, and that such failure or action caused the loss.

(5) The rights of action authorized by this subsection shall be the exclusive remedy under this chapter available to any person who sustains a loss as a result of (A) the alleged failure by a registered entity or registered futures association or by any officer, director, governor, committee member, or employee to enforce any bylaw, rule, regulation, or resolution referred to in paragraph (1) or (2) of this subsection, or (B) the taking of action in enforcing any bylaw, rule, regulation, or resolution referred to in this subsection that is alleged to have violated this chapter, or any Commission rule, regulation, or order.

(c) Jurisdiction; statute of limitations; venue; process

The United States district courts shall have exclusive jurisdiction of actions brought under this section. Any such action shall be brought not later than two years after the date the cause of action arises. Any action brought under subsection (a) of this section may be brought in any judicial district wherein the defendant is found, resides, or transacts business, or in the judicial district wherein any act or transaction constituting the violation occurs. Process in such action may be served in any judicial district of which the defendant is an inhabitant or wherever the defendant may be found.

(d) Dates of application to actions

The provisions of this section shall become effective with respect to causes of action accruing on or after

the date of enactment of the Futures Trading Act of 1982 [January 11, 1983]: *Provided*, That the enactment of the Futures Trading Act of 1982 shall not affect any right of any parties which may exist with respect to causes of action accruing prior to such date.

Supreme Court, U S
FILED
JAN 26 2010
OFFICE OF THE CLERK

No. 09-517

In the Supreme Court of the United States

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC AND PIMCO FUNDS,

Petitioners,

v.

RICHARD HERSHEY, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY TO BRIEF IN OPPOSITION

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INTRODUCTION

The Seventh Circuit's decision in this case fundamentally alters the gateway standards governing the all-important class certification determination in a way that not only conflicts with decisions of this Court and other circuits, but overwhelmingly favors class action plaintiffs. Indeed, in just the few months since the Seventh Circuit's ruling, plaintiffs already have been "ma[king] much"[1] of the decision in arguing for class certification. Respondents—who believe that "more" class actions are "needed" and suggest that the "'hydraulic pressure'" that class certification places on defendants to settle is "'more myth than reality,'" Opp.37-38—have thrown up everything they can in an attempt to divert this Court's attention from the undeniably important questions presented. But upon analysis, respondents' litany of objections only underscores the need for plenary review.

Moreover, in many respects the brief in opposition is most remarkable for what it does not say. For example, respondents do not deny that the Seventh Circuit placed on *defendants* the burden of demonstrating that certification of this overbroad class was improper. That ruling directly conflicts with decisions of this Court and other circuits, Pet.17-21, and respondents do not defend it. And, as *amicus* DRI has explained (at 13), "[i]t goes without saying that plaintiffs in the Seventh Circuit will take full advantage of this shift"—and "already are doing so."

Respondents also do not defend the Seventh Circuit's remarkable holding that a class may be drawn

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[1] *Reed v. Advocate Health Care*, No. 06 C 3337, 2009 U.S. Dist. LEXIS 89576, at *21 n.7 (N.D. Ill. Sept. 28, 2009).

so broadly that it embraces numerous members who actually *benefited* from the alleged misconduct. Instead, they suggest that this issue is not presented because *all* class members purportedly were injured. Opp.19-27. That contention fails as a matter of fact and law. But it is also beside the point. The Seventh Circuit decided this case based on the premise that the class *does* contain numerous members who were uninjured "net gainers" and squarely held that the certification of such a class was proper under Rule 23. Pet.App.12a-13a. That holding directly conflicts with the decisions of other circuits and merits review.

Respondents also do not seriously defend the Seventh Circuit's holding that obvious inherent conflicts of interest within a class can be disregarded at the class certification stage. Instead, they posit that many lower courts routinely ignore intra-class conflicts to promote use of the class-action device (Opp.30-36)—in direct contravention of this Court's decision in *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 613 (1997). That admission simply underscores why this Court's review is necessary.

ARGUMENT

1. As explained in the petition, this case presents several fundamental issues concerning the standards governing the class certification decision—the pivotal event in most class actions. Respondents do not even attempt to defend the Seventh Circuit's ruling that *defendants* bore the burden of proof to establish that certification was not warranted. Pet.App.14a. That ruling directly conflicts with decisions of this Court and other circuits. Pet.20-21. And as *amicus* DRI explains, that reallocation of the burden of proof—along with the court of appeals' related failure to subject the

certification request to the requisite "rigorous analysis," *Gen. Tel. Co. of the Sw. v. Falcon*, 457 U.S. 147, 161 (1982); *see* Pet.17-20—"fundamentally alters the Rule 23 certification process." DRI Br.13-14.

As to the Seventh Circuit's failure to insist on the requisite inquiry before certification, respondents assert that the "'circuits agree'" that "'a searching inquiry regarding the Rule 23 criteria'" is required. Opp.28; *see also* Opp.29-30. But the cases cited by respondents simply underscore the conflict created by the decision below, which affirmed class certification based solely on unproven allegations and the court's own speculation and armchair economics, Pet.19-20—and then wrongly put the burden on defendants to prove that certification was not warranted.

2. Nor do respondents seriously defend the Seventh Circuit's remarkable ruling that Rule 23 permits the certification of a class drawn so broadly that it encompasses numerous members who not only were not injured by—but actually *benefited* from—the alleged misconduct. Pet.App.12a-14a.

The Seventh Circuit acknowledged that the proposed class includes members who "were not injured at all," Pet.App.8a, and, indeed, "probably were net gainers from the alleged manipulation," Pet.App.12a, but held that fact to be legally irrelevant, Pet.App.10a. Of course, many classes may include some members who in the end cannot prove that they were injured. But the Seventh Circuit held that Rule 23 permits the certification of a class that includes numerous persons who, even accepting all allegations as true, cannot possibly have suffered injury because they *benefited* from the alleged wrongdoing. *See* Pet.11-12. That decision directly conflicts with the

decisions of other circuits barring "class certification where some class members derive[d] a net economic benefit from the very same conduct alleged to be wrongful." *Valley Drug Co. v. Geneva Pharms., Inc.*, 350 F.3d 1181, 1190 (11th Cir. 2003); *see* Pet.12-15.[2]

Certiorari is warranted to resolve that conflict. Certifying such an "overbroad" class not only unjustly increases the "pressure to settle" but contravenes the Rules Enabling Act and this Court's decisions (*e.g.*, *Amchem*, 521 U.S. at 613). *See* Pet.15-17. Indeed, as DRI has explained (at 4), the decision below "renders Rule 23 a vehicle for expanding substantive rights by permitting parties to participate in class actions, and obtain monetary or other relief, when they do not satisfy all of the essential requirements for asserting the underlying cause of action."

Respondents have no real response. Instead, they try to change the subject by taking issue with the "premise that there are 'uninjured' members in the class." Opp.19. But the Seventh Circuit decided that certification was proper based on that very premise. And other courts are already citing the Seventh Circuit's decision for the proposition that "[c]lass certification is not precluded simply because a class may include persons who have not been injured by the defendant's conduct." *Mims v. Stewart Title Guar. Co.*,

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[2] Respondents attempt to distinguish the supposedly "very different" facts of the conflicting *Valley Drug* decision. Opp.25-26. They argue that there plaintiffs constituting over half the class had cost-plus sales contracts which made them "net gainers" who benefited from defendants' antitrust overcharges. Yet the facts here are analogous because the record also shows that a majority of class members for whom there is data benefited from the alleged price manipulation. Pet.5,12.

No. 09-10127, 2009 U.S. App. LEXIS 26842, at *21-22 (5th Cir. Dec. 9, 2009); *see also, e.g., Allen v. Am. Honda Motor Co.*, No. 06 C 5932, 2009 U.S. Dist. LEXIS 115185, at *18 (N.D. Ill. Dec. 8, 2009) ("As the Seventh Circuit recently explained, 'a class will often include persons who have not been injured by the defendant's conduct ....'").[3] In deciding this case, the Court need only say—as it often does—that the court of appeals' decision was wrong as a matter of law based on its own terms.

Regardless, the record irrefutably shows that the Seventh Circuit's premise concerning uninjured class members was correct. *See* Pet.11-12. For example, respondents' own expert reports establish that class representative Hershey and "a majority of the class members for whom there is trading data in the record actually benefited from the alleged manipulation." Pet.5, 12. Respondents do not deny those points, and they therefore must be accepted. S. Ct. R. 15.2. Any remaining uncertainty just shines a spotlight on the fundamental problem—that the district court failed to engage in the requisite "rigorous analysis" before certification, which must include a genuine factual inquiry into the *extent* to which the class is overbroad. *See* Pet.17-20.

Respondents' real argument is legal, not factual. They argue that, regardless of which class members gained as a result of the alleged misconduct, *everyone* in the class suffered some abstract legal injury under

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[3] Class action plaintiffs are going even further and arguing that the decision below authorizes certification of classes containing "individuals without claims" at all. Pls.' Reply Mem., *Moss v. Cent. United Life Ins. Co.*, No. 09-4030-CV-C-NKL, 2009 WL 3639057 (W.D. Mo. Sept. 9, 2009) (citing decision below).

the CEA by virtue of having paid an artificially high price to liquidate a short position. Opp.20-22.[4] In certifying the class, the district court essentially adopted the same position. Pet.App.24a-27a. But the Seventh Circuit correctly rejected that theory, Pet.App.14a—and with good reason. It is flatly inconsistent with *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005), which holds that economic harm must be determined by examining *both* sides of a financial transaction, and that a person who purchases stock at an artificially elevated price suffers no injury at all if he also *sells* that stock at a similarly inflated price. *Id.* at 342-43, 347; Pet.App.14a.

There is no plausible way to distinguish *Dura* here. Indeed, the requirement of proving economic loss is even more obvious here than in *Dura* because the underlying cause of action explicitly limits the class of potential plaintiffs to those who suffered "actual damages." 7 U.S.C. §25. And, as explained (Pet.3, 16), the history of the CEA's express cause of action underscores that Congress meant what it said.

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[4] Respondents suggest that petitioners waived an objection to the presence of uninjured traders in the class. Opp.3 n.2. But petitioners raised this issue from the outset, Opp. to Class Cert.4-10 (N.D. Ill. Docket No. 99), presented it to the Seventh Circuit, *see, e.g.*, Appellants' Br.34 (7th Cir. Sept. 15, 2008), and the Seventh Circuit squarely decided it, Pet.App.10a-14a. Nor did petitioners "concede[]" at oral argument that the class would be proper if limited to those who "opened short positions prior to May 9." Opp.12. When pressed at argument for a class definition that might pass muster, counsel suggested that a class of "traders who establish[ed] a short position before May 9, liquidated during the class period, *and did not otherwise trade* [would] essentially eliminate the net gainers and reduce the conflicts to a feasible level." 2009 WL 925914 (Apr. 1, 2009) (unofficial transcript). Such a class is far different than the one certified below. Pet.11-12.

In any event, this legal issue is also beside the point because, as noted, the Seventh Circuit's decision is based on the premise that the class includes numerous members who were uninjured. The court's conclusion that Rule 23 permits the certification of such an overbroad class warrants certiorari. *See* DRI Br.6-8.

3. Certiorari is also warranted to review the Seventh Circuit's decision that certification was proper despite the irrefutable fact that the class was beset by severe internal conflicts of interest—including class members who bought and sold opposite each other on the same days. Pet.21-30.[5] Respondents acknowledge that the conflicts problem has troubled the lower courts for decades. Opp.30-36; Pet.28-30. But they suggest that this case is not a suitable vehicle to address the issue.[6] They are wrong again.

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[5] Respondents' assertion that petitioners waived any objection to the "adequacy of class counsel" (Opp.16-17 & n.11) is beside the point. Petitioners' Rule 23(a)(4) argument hinges on the adequacy of the class *plaintiffs* as representatives of absent class members—an issue vigorously argued below, *see, e.g.*, Appellants' Br.41-48; Appellees' Br.46-51 (7th Cir. Nov. 14, 2008); Opp to Class Cert.10-17, and decided by the Seventh Circuit, Pet.App.15a-16a.

[6] The "matrix" (Opp.34-35) concocted by respondents is both irrelevant and unpersuasive. All but one of respondents' cases predate *Dura* and all rest on the erroneous premise that differences among plaintiffs were limited to variations in the amount of damages, rather than the fact of injury. The two S.D.N.Y. cases applied a class certification standard later rejected by the Second Circuit. *See In re IPO Sec. Litig.*, 471 F.3d 24, 35 & n.5 (2d Cir. 2006). And *In re Soybeans Futures Litigation*, Nos. 89 C 7009, 90 C 1138, 1993 U.S. Dist. LEXIS 18738, at *2 (N.D. Ill. Dec. 27, 1993), involved stipulated subclasses drawn because the court *rejected* the proposed class for reasons like those advanced by petitioners here.

This case is an ideal vehicle to address this important question. The undeniable facts present the conflicts problem in an unusually sharp form, Pet.23-24, yet the Seventh Circuit nevertheless squarely held that certification was proper without *any* inquiry into the extent of such conflicts, Pet.App.15a-16a.

Respondents suggest that, because this is a CEA case, it is factually distinguishable from contrary authority that prohibits certification in the face of obvious conflicts under antitrust, securities, or personal injury law, such as *Amchem*, 521 U.S. at 625-28, and *Valley Drug*, 350 F.3d at 1184-89. Opp.30-36. But the Seventh Circuit did not in any way rest its holding on the CEA. It announced a general principle applicable to *all* class certification decisions under Rule 23, and held that inquiry into the extent of intra-class conflicts at the class certification stage is "premature." Pet.App.16a. In so holding, the court relied on cases involving consumer finance, securities law, and employment discrimination. Pet.App.15a-16a.

The conflicts in this case relate to class members' starkly differing interests in proving the level of alleged price "artificiality" at particular times.[7] Price artificiality is also at the heart of most securities and antitrust cases. All of the same problems can arise, for

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[7] In a "Corrected" Brief in Opposition (at 40 n.21) filed more than a week late, respondents attempt to take issue—in a new footnote improperly added to the brief—with the petition's characterization of the obvious conflicts among class members. Respondents' untimely effort to supplement their response should be rejected, but in any event, any dispute over this issue further underscores the need for guidance on whether the district court was required to make findings on the extent of the intra-class conflict *before* certification. *See* Pet.27-29.

example, with a securities class defined so broadly that it includes "in and out" traders with conflicting interests in whether a particular public disclosure corrected pre-existing artificiality in the stock price. Accordingly, numerous courts have recognized that the CEA and the securities acts should be construed consistently wherever possible. *See, e.g., Leist v. Simplot*, 638 F.2d 283, 298 n.14 (2d Cir. 1980), *aff'd, Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982); *FDIC v. UMIC, Inc.*, 136 F.3d 1375, 1384 n.4 (10th Cir. 1998); *Monieson v. CFTC*, 996 F.2d 852, 858-60 (7th Cir. 1993).

Respondents argue that purchaser/seller conflicts should be ignored in the interest of facilitating broad class certification and that the concerns identified in cases like *Valley Drug, Langbecker v. Electronic Data Sys. Corp.*, 476 F.3d 299 (5th Cir. 2007), and *In re Seagate Technology II Securities Litigation*, 843 F. Supp. 1341 (N.D. Cal. 1994), have been "discredited." Opp.30-33. Respondents are correct that the lower courts are divided on how to deal with intra-class conflicts at the certification stage. But that is precisely why this Court's review is needed.

As *Seagate* and its progeny have recognized, intra-class conflicts—including purchaser/seller conflicts like those present here—are directly relevant to several of Rule 23's criteria and often cannot be redressed in any practical way later (through "subclasses" or otherwise). And, as courts have held, a trial court should not certify a class in the face of such conflicts without *at least* "requir[ing] the named representatives to bring forth evidence ... that no fundamental conflict exists among the class members." *Valley Drug*, 350 F.3d at 1196; *see* Pet.27. The district court here refused to do

that, and the Seventh Circuit's decision likewise gives district courts the green light to ignore intra-class conflicts at the certification stage, rather than carefully to analyze their scope and significance.

4. Finally, respondents do not seriously contest the importance of the questions presented. Instead, they suggest that the particular type of claim underlying this class action makes it an unsuitable vehicle to resolve those issues. *See* Opp.36-39. That contention is clearly wrong. As DRI explains (at 2), the issues presented by this case "can have considerable, and even dispositive, impact in numerous types of class actions, including large-scale securities, antitrust, and commodities cases." *See id.* at 7-8 & nn.3-4. Even the early returns bear that out. Class plaintiffs and lower courts already are relying on the decision below in a wide variety of contexts.[8] And that makes perfect sense—the broad legal holdings reached by the

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[8] *See, e.g., Mims*, 2009 U.S. App. LEXIS 26842 (Real Estate Settlement Procedure Act); *Allen*, 2009 U.S. Dist. LEXIS 115185, at *18-19 (state law breach of express and implied warranties); *Reyher v. State Farm Mut. Auto. Ins. Co.*, No. 07-CV-4446, 2009 Colo. App. LEXIS 1968, at *22-23 (Colo. Ct. App. Dec. 24, 2009) (insurance law); and Respondents' Mem. of Law in Supp. of Mot. to Exclude Expert Opinion of Monica Noether, *In re Evanston Nw. Healthcare Corp. Antitrust Litig.*, No. 07-cv-4446, 2009 WL 4883940 (N.D. Ill. Dec. 14, 2009) (antitrust). Indeed, in *Evanston*, an antitrust case, respondents' counsel themselves invoked the decision below to argue that a report demonstrating "that a number of members of the proposed Class did not suffer any impact from the anti-competitive behavior" is irrelevant at the class certification stage. *Id.*

Seventh Circuit below on the standards governing class certification are in no way limited to the CEA.[9]

* * *

Adherence to proper procedural practice in class action litigation is extraordinarily important because of the enormous potential impact of class actions on defendants and the judicial system. The decision below unsettles the standards governing class certification in several fundamental respects. All the traditional criteria for certiorari are met, including "well-defined splits of authority," DRI Br.2-3, and this case is an excellent vehicle to provide long overdue guidance on the important and recurring questions presented. Certiorari, in short, is plainly warranted.

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[9] Respondents' reference to the "interlocutory" posture of this case is a red herring. Opp.1. The decision below represents the final word on whether certification was proper. Moreover, Rule 23(f) was added precisely to authorize interlocutory appeals of class certification orders because of the important interests at stake. *See* Fed. R. Civ. P. 23 advisory committee notes, 1998 Amendments.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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IN THE

Supreme Court of the United States

PACIFIC INVESTMENT MANAGEMENT COMPANY LLC AND PIMCO FUNDS,

Petitioners,

v.

RICHARD HERSHEY, *et al.*,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

MOTION FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE* AND BRIEF OF DRI – THE VOICE OF THE DEFENSE BAR AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

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MOTION OF DRI – THE VOICE OF THE DEFENSE BAR FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

DRI – the Voice of the Defense Bar hereby requests, pursuant to Rule 37.2(b) of the Rules of this Court, leave to file the accompanying brief as *amicus curiae* in support of petitioners. DRI obtained the consent of petitioners. Petitioners' letter of consent has been filed with the Clerk of the Court. Respondents, however, withheld their consent from the filing of this brief in support of the petition.

DRI offers this brief because the issues to be decided affect the interests of DRI and its members.

DRI is an international organization that includes more than 22,000 attorneys involved in the defense of civil litigation. DRI is committed to enhancing the availability, effectiveness, and professionalism of defense attorneys. Because of this commitment, DRI seeks to address issues germane to defense attorneys, their clients, and the civil justice system. DRI has long been a voice in the ongoing effort to make the civil justice system more fair, efficient, and – especially on national issues – consistent. DRI has previously filed *amici* briefs with the Court in cases concerning the civil justice system. See, *e.g.*, *Stolt-Nielsen S.A.* v. *AnimalFeeds Int'l*, No. 08-1198 (filed Sept. 4, 2009); *Mohawk Indus., Inc.* v. *Carpenter*, No. 08-678 (filed May 4, 2009); *Wyeth* v. *Levine*, 129 S. Ct. 1187 (2009) (filed June 3, 2008).

The questions presented by this case – whether and to what extent Fed. R. Civ. P. 23 permits the certification of classes that include uninjured plaintiffs and whether the burden can be placed on defendants to prove that the requirements of Rule 23 are not satisfied – are issues of recurring importance for DRI's members and their clients. DRI's members frequently are involved in putative class actions and it is critically important to them and their clients that Rule 23 not be interpreted in a manner that impermissibly affects and enlarges substantive rights. It is equally important to DRI's members and their clients that a uniform rule of law be applied across the country.

DRI therefore has a vital interest in the issues presented in this case, and its views can assist the Court in deciding whether certiorari should be granted. For the foregoing reasons, DRI's Motion for

Leave to File a Brief as *Amicus Curiae* in Support of Petitioners should be granted.

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INTEREST OF *AMICUS CURIAE* DRI[1]

Amicus curiae DRI – the Voice of the Defense Bar is an international organization that includes more than 22,000 attorneys involved in the defense of civil litigation. DRI is committed to enhancing the availability, effectiveness, and professionalism of defense attorneys. Because of this commitment, DRI seeks to address issues germane to defense attorneys, their clients, and the civil justice system. DRI has long been a voice in the ongoing effort to make the civil justice system more fair, efficient, and – especially on national issues – consistent.

To promote its objectives, DRI participates as *amicus curiae* in cases that raise issues of vital concern to its membership, their clients, and the judicial system. This is just such a case. DRI believes that resolution of the important federal class action issues that the petition squarely presents is critical because the circuits have fractured over

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[1] Pursuant to Supreme Court Rule 37.6, *amicus curiae* DRI states that Sidley Austin LLP is one of the law firms that is representing petitioners in the district court. Sidley Austin's appellate group was retained by DRI to prepare this brief and the appellate attorneys who prepared this brief had no substantive discussions with the attorneys working on the litigation. Neither petitioners, nor any other entity or person, aside from *amicus curiae*, its members, and its counsel, made any monetary contribution toward the preparation or submission of this brief. Pursuant to Supreme Court Rule 37.2, counsel of record for all parties received timely notice of *amicus curiae*'s intent to file this brief. DRI obtained the consent of petitioners. Petitioners' letter of consent has been filed with the Clerk of the Court. Respondents, however, withheld their consent from the filing of this brief in support of the petition.

whether and to what extent Fed. R. Civ. P. 23 permits the certification of classes that include uninjured plaintiffs and whether the burden can be placed on defendants to prove that the requirements of Rule 23 are not satisfied. These issues can have considerable, and even dispositive, impact in numerous types of class actions, including large-scale securities, antitrust, and commodities cases. Because class action certification is an issue of particular significance to defendants, DRI's members are frequently confronted with the precise issues raised by petitioners, and their clients are affected by the lack of a clear, uniform rule.

DRI opposes the standards adopted by the court of appeals that permit the certification of classes that include uninjured plaintiffs and that impose on defendants the burden of showing that class certification is improper. But what is of paramount importance now is that this Court grant review to resolve the conflict in the courts of appeals. Adoption of a uniform rule that governs all future federal class action certification proceedings is essential to prevent unseemly and unfair forum-shopping and to bring consistency and predictability to class action certification.

INTRODUCTION

Petitioners have presented a thorough statement of the case, which DRI will not repeat, and have demonstrated persuasively the split among courts of appeals on the issues presented, as well as various reasons why this Court should grant the petition. *Amicus* DRI believes that review of these issues is fully warranted for the reasons articulated by petitioners and submits this brief to highlight

significant additional reasons why this Court should grant certiorari.

This case squarely implicates well-defined splits of authority among the courts of appeals on how to interpret Rule 23. These conflicts present a compelling case for intervention by this Court because they fall squarely within the Court's traditional duty to ensure uniformity on issues of federal court procedure. The need for review is even more urgent because the court of appeals interpreted Rule 23 in a manner that is contrary to the clearly expressed purposes embodied in the 2003 amendments to the Rule and would impermissibly affect and enlarge substantive rights. If allowed to stand, the court of appeals' decision will fundamentally alter the operation of Rule 23 in the Seventh Circuit, as well as lead to unseemly and unfair forum-shopping. The Court should grant certiorari to prevent these results and to establish uniformity in an important area of federal procedure.

REASONS FOR GRANTING THE PETITION

I. THE CONFLICT CONCERNING WHETHER RULE 23 PERMITS THE CERTIFICATION OF CLASSES THAT INCLUDE UNINJURED PLAINTIFFS WARRANTS THIS COURT'S REVIEW.

As the petition demonstrates, the decision below squarely conflicts with the decisions of other circuits holding that class certification is not proper where some class members incurred no injury or even derived a net economic benefit from the same conduct that the named plaintiffs allege injured them. Pet. 11-15. Indeed, until the decision below, no circuit had approved certification of such a class. *Id.* at 12.

Here, the Seventh Circuit acknowledged that "some of the class members probably were net gainers from the alleged manipulation," but nevertheless upheld the district court's decision certifying a class action on the ground that it "has not yet been shown" that the class definition was "clearly" overbroad. Pet. App. 12a; see also *id.* at 13a (acknowledging that "the class definition may be too broad"). The Seventh Circuit offered its own speculation that not "many" of the class members were net gainers, *id.*, but it failed to address any of the trading data in the record which suggests – under the analysis of *plaintiffs'* own experts – that a *majority* of the class members were in fact net gainers. See Pet. 5. The court of appeals' ruling warrants review because it would impermissibly affect and enlarge substantive rights, and is unfaithful to the purposes of Rule 23.

1. The court of appeals' ruling improperly renders Rule 23 a vehicle for expanding substantive rights by permitting parties to participate in class actions, and obtain monetary or other relief, when they do not satisfy all of the essential requirements for asserting the underlying cause of action. This Court unequivocally has held that "Rule 23's requirements must be interpreted in keeping with Article III constraints, and . . . shall not abridge, enlarge or modify any substantive right." *Amchem Prods., Inc.* v. *Windsor*, 521 U.S. 591, 613 (1997) (internal quotation marks omitted); *Ortiz* v. *Fibreboard Corp.*, 527 U.S. 815, 845 (1999) ("[N]o reading of [Rule 23] can ignore the [Rules Enabling] Act's mandate that rules of procedure shall not abridge, enlarge or

modify any substantive right") (internal quotation marks omitted).[2]

The standard adopted by the Seventh Circuit, however, permits Rule 23 to do exactly that. As petitioners demonstrated, Pet. 16, injury or "actual damages" is an essential element of the private right of action under the Commodities Exchange Act ("CEA"), 7 U.S.C. § 25(a)(1). Stated differently, uninjured parties have no right to bring a private action under the CEA. By allowing such uninjured parties to participate in a class, the Seventh Circuit has applied Rule 23 to enlarge the substantive rights of those uninjured parties. When uninjured plaintiffs attempt to commence individual CEA actions in federal court, their meritless actions can readily be screened out at the motion to dismiss stage or after basic discovery. The certification of classes that include uninjured plaintiffs, however, leaves defendants without any practical or early means of identifying and eliminating uninjured plaintiffs. This expansion of the uninjured plaintiffs' rights – by giving them the ability to "free ride" on the legitimate claims of injured plaintiffs – is a result that not only contravenes the purposes of the Rules Enabling Act,

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[2] *See also McLaughlin* v. *American Tobacco Co.*, 522 F.3d 215, 231 (2d Cir. 2008) ("federal rules of procedure, such as Rule 23, cannot be used to abridge, enlarge or modify any substantive right") (internal quotation marks omitted); *Cummings* v. *Connell*, 402 F.3d 936, 944 (9th Cir. 2005) ("It is axiomatic that Rule 23 cannot abridge, enlarge or modify any substantive right of any party to the litigation") (internal quotation marks omitted); *Blaz* v. *Belfer*, 368 F.3d 501, 504 (5th Cir. 2004) ("A class action is merely a procedural device; it does not create new substantive rights") (internal quotation marks omitted).

but also wholly undermines the limits that Congress imposed on the private right of action.

It is no answer to suggest, as the court of appeals did, that uninjured plaintiffs can be eliminated at the damages stage of the class action. Pet. App. 7a-8a (suggesting that uninjured plaintiffs will either not submit claims for damages or will submit claims that ultimately will be rejected). For one thing, many – if not most – class actions never get that far. As petitioners demonstrated, and as even the court of appeals below acknowledged, the issue of class certification is of "touchstone importance" in complex civil cases because the certification of a putative class induces many defendants to settle. Pet. 1, 8, 30; see also Pet. App. 11a (acknowledging "the *in terrorem* character of a class action" and the pressure on defendants to "settle rather than to bet the company"). Indeed, the pressure to settle is even greater when the class is overbroad and defendants face potential liability to numerous uninjured plaintiffs. When a class action that includes uninjured plaintiffs results in a monetary settlement – as will often be the case – uninjured plaintiffs necessarily share in the settlement. This means that they recover under a statute that expressly was designed *not* to provide them with any cause of action, and from parties who did *not* injure them. This result is patently unjust and nothing in Rule 23 supports, much less requires, such an outcome.

Moreover, even in the infrequent case where a complex class action reaches a damages phase, and further proceedings theoretically could be used to screen out uninjured plaintiffs, defendants still would be required to bear the enormous effort and expense of litigating the overbroad class action to conclusion

and eliminating improper plaintiffs only at the final phase. In addition, overbroad class actions can impose substantial collateral burdens on defendants, such as adverse publicity that can harm their reputation and public disclosure obligations that can unfairly impact their stock price. The prospect of defendants having to bear these substantial costs and litigation burdens itself contravenes Congress's purposes in limiting the availability of the cause of action in the first instance to injured parties.

The litigation burden would be particularly onerous in cases like this one, where the existence of injury must be determined on a plaintiff-by-plaintiff basis. Indeed, when faced with the prospect of such individualized injury determinations, federal courts often conclude that class treatment is not appropriate. See, *e.g.*, *Alabama* v. *Blue Bird Body Co.*, 573 F.2d 309, 327-28 (5th Cir. 1978) (class may not be certified unless injury-in-fact can be established on a common basis); *Bell Atl. Corp.* v. *AT&T Corp.*, 339 F.3d 294, 302-03 (5th Cir. 2003); *Valley Drug Co.* v. *Geneva Pharms., Inc.*, 350 F.3d 1181, 1190-91 (11th Cir. 2003); *Pickett* v. *Iowa Beef Processors*, 209 F.3d 1276, 1280-81 (11th Cir. 2000). The Seventh Circuit's contrary conclusion here – that a class should be certified and injury determinations left for later case-by-case adjudication – demonstrates how far out of step it is with other circuits.

This issue extends far beyond class actions that arise under the CEA. The same issue arises under numerous federal statutes that require proof of injury

as an essential element of a private cause of action.[3] It also arises under putative Rule 23 class actions that are based on state statutes that require proof of injury as an essential element of a private cause of action, such as deceptive and unfair trade practice laws.[4] In addition, this issue is implicated in putative class actions involving state common law causes of action that require proof of injury, such as negligence and other theories commonly used in products liability class actions – a considerable category of large-scale cases in the federal courts. Indeed, given ever-expanding uses of Rule 23, it would be hard to find a more compelling example of a clear division in the circuits that affects numerous types of cases and, as a result, warrants this Court's attention.

2. Aside from the impact of the court of appeals' ruling on substantive rights, its interpretation of Rule 23 to permit named plaintiffs to obtain cer-

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[3] *See, e.g.*, 15 U.S.C. § 78u-4(b)(4) (elements of private securities fraud actions include a "loss" and "[l]oss causation"); 15 U.S.C. § 15(a) (private damages action under the antitrust laws is only available to a person "injured in his business or property" by reason of the alleged violation); 18 U.S.C. § 1964(c) (civil RICO action only available to a person "injured in his business or property" by reason of the alleged violation).

[4] *See, e.g.*, N.Y. Gen. Bus. Laws § 349(h) (private damages action under New York's deceptive trade practices law available to persons "injured" by reason of the violation); Mass. Gen. Laws ch. 93A, §§ 2, 9(1) (same for Massachusetts' deceptive trade practices law); 815 Ill. Comp. Stat. §§ 505/2, 505/10a (private damages action under Illinois' unfair trade practices law available to persons who suffer "actual damage" by reason of the violation).

tification of overbroad classes that include plaintiffs who ultimately cannot recover is contrary to the purposes of the Rule. As Rule 23 has evolved, a central purpose has been to prevent class litigation from going forward with overbroad and ill-defined classes that – after the expenditure of significant resources by the parties and the court – ultimately have to be narrowed, or even decertified.

For example, Rule 23 was amended in 2003 to remove the requirement that the court determine whether to certify a class "as soon as practicable after commencement of an action," and replace it with the requirement that the determination be made "at an early practicable time." See Fed. R. Civ. P. 23 cmt. to 2003 amendments. The Advisory Committee explained that the "as soon as practicable" requirement failed to capture "the many valid reasons that may justify deferring the initial certification decision." *Id.* In particular, "[t]ime may be needed to gather information necessary to make the certification decision." *Id.* In addition, Rule 23 also was amended in 2003 to eliminate "conditional" class certification. The Advisory Committee explained that "conditional" certification was being abolished because "[a] court that is not satisfied that the requirements of Rule 23 have been met should refuse certification until they have been met." *Id.*

The purpose of both of these rule changes was to prevent named plaintiffs from seeking certification of classes that they know little about, and instead require them to investigate the potential plaintiff pool and seek certification of well-tailored classes that satisfy the requirements of Rule 23. The court of appeals' rule, however, will have the opposite effect. It permits named plaintiffs to seek and obtain

certification of very expansive classes of plaintiffs, before they have even come to grips with who was potentially harmed by a defendant's alleged conduct and who was not. This turns the class action device into a very wide net for hauling defendants into federal court, including defendants whom further inquiry will reveal should not have been there in the first place. At the very least, it increases the risk that district courts and parties will have to devote considerable time and resources to narrowing, subdividing or even decertifying classes that have been certified – an outcome that in many cases could have been avoided by careful inquiry in the first instance. The court of appeals' interpretation of Rule 23 therefore undermines the Advisory Committee's intent to ensure that class certification determinations are based upon adequate information so that the actions that are certified for class treatment are consistent with the purposes of the rule. For this reason as well, the Court should grant the petition.

II. THE CONFLICT CONCERNING WHETHER THE BURDEN CAN BE PLACED ON DEFENDANTS TO SHOW THAT CLASS CERTIFICATION IS IMPROPER WARRANTS THIS COURT'S REVIEW.

The petition also demonstrates that the decision below squarely conflicts with the decisions of other circuits holding that plaintiffs bear the burden of showing that class certification and the proposed class are proper under Rule 23. Pet. 20-21. Indeed, other courts of appeals have deemed it reversible error for the burden to be placed on a defendant to show that class certification is improper. *Id.* (citing *In re Am. Med. Sys., Inc.*, 75 F.3d 1069, 1086 (6th Cir. 1996)); see also *Berger* v. *Compaq Computer Corp.*,

257 F.3d 475, 481 (5th Cir. 2001) (describing the district court's inversion of the burden of proof as "unquestionably . . . incorrect" and "unsettling"). Here, however, the court of appeals not only rejected petitioners' argument that the proposed class was too broad to satisfy the Rule 23 requirements on the ground that *petitioners* "failed to justify . . . the extent to which the class definition may be too broad," Pet. App. 13a, but further faulted petitioners for failing to "depose a random sample of class members to determine how many were net gainers from the alleged manipulation," *id.* at 14a.

This conflict warrants this Court's attention. As an initial matter, the Seventh Circuit's holding that defendants must *disprove* the appropriateness of class certification not only conflicts with the holdings of other courts of appeals, but also conflicts with decisions of this Court and with the uniform view of commentators. As petitioners noted, Pet. 20, this Court itself has held that "*parties seeking class certification* must show that the action is maintainable under Rule [23]," *Amchem*, 521 U.S. at 614 (emphasis added). Along with the other courts of appeals that have faithfully applied this Court's holding, commentators agree that plaintiffs have the burden of showing that all Rule 23 requirements are satisfied. See, *e.g.*, 7A Wright, Miller & Kane, *Federal Practice and Procedure: Civil* § 1759, at 122 (3d ed. 2005) ("The party who is invoking Rule 23 has the burden of showing that all of the prerequisites to utilizing the class action procedure have been satisfied"); 5 James W. Moore, *Moore's Federal Practice* § 23.83, at 23-383 (3d ed. 2009) ("The party seeking class certification has the burden of demonstrating that all the requirements for a class

action under Rule 23(a) and (b) have been met and that the action should be certified as a class action."); 3 Alba Conte & Herbert Newberg, *Newberg on Class Actions* § 7.17, at 59 (4th ed. 2002) ("The proponent of class certification bears the burden of showing that the action is proper for class certification."); 1 Joseph M. McLaughlin, *McLaughlin on Class Actions* § 3:10 (5th ed. 2008) ("The burden of proving each of the requisite elements of Rule 23 is on the party seeking certification, and failure to prove any element precludes certification.").

It is not surprising that the Seventh Circuit stands alone on this issue because its standard undercuts the purposes of Rule 23. As noted, Rule 23 was amended in 2003 to eliminate "conditional" class certification. This change eliminated the ability of named plaintiffs to seek and obtain "conditional" certification of overbroad and ill-defined classes based upon cursory investigation of the potential class members, only to have the classes ultimately revealed to be unsuitable and decertified – after the expenditure of considerable resources by the trial court and the parties. The Seventh Circuit's inversion of the burden of proof, however, revives the evils of conditional certification because it permits named plaintiffs to seek certification of overbroad classes without proper inquiry, and then leaves it to defendants to prove how and why the classes are overbroad. The court of appeals' standard therefore wholly vitiates the intent of the Advisory Committee to place the onus on named plaintiffs to evaluate the potential plaintiff pool and then propose properly tailored classes that satisfy the requirements of Rule 23.

The Seventh Circuit's standard also fundamentally alters the Rule 23 class certification process, which, as petitioners have demonstrated, Pet. 1, 8, 30, often is dispositive in large-scale class actions. Given that class actions already induce "blackmail settlements" in the circuits that properly place the burden on plaintiffs to show that all of the Rule 23 requirements are satisfied, see Henry J. Friendly, *Federal Jurisdiction: A General View* 120 (1973), the dynamics that induce such settlements will be overwhelmingly powerful in the Seventh Circuit, which has shifted this substantial burden to defendants. It goes without saying that plaintiffs in the Seventh Circuit will take full advantage of this shift; indeed, as petitioners point out, Pet. 32, they already are doing so.

The costs of the Seventh Circuit's approach are substantial, as this case illustrates. The court of appeals acknowledged that "the [putative] class has more than a thousand members" and that "determining the value" of the class members' claims would have to be done on an individualized basis. Pet. App. 11a-12a. Yet it held that petitioners should have deposed a sufficiently large sample of the putative class (and presumably sought and reviewed supporting documents and financial records for each and every putative plaintiff) as to permit a reliable estimate – presumably by one or more experts – of the number of noninjured members in *plaintiffs'* proposed class. Such a detailed and sophisticated study in a complex commodities trading case – essentially duplicating the fact-gathering and analysis the plaintiffs would have to undertake in the damages phase of an eventual trial – would consume substantial time and resources.

Requiring *defendants* to shoulder this burden at the *class certification* stage of putative Rule 23 actions therefore fundamentally alters their settlement incentives – particularly in complex securities, antitrust, and commodities cases. *See* Pet. App. 11a (acknowledging that this lawsuit involves "a multi-hundred-million-dollar claim" that will require "protracted and costly litigation"). In such cases, the very act of opposing class certification will be daunting for many defendants, or even cost-prohibitive. Thus, not only will defendants in such cases face enormous pressure to settle in the circumstance where a class is certified, but they also will face pressure to reach early settlements with plaintiffs solely to avoid contentious and costly class certification proceedings. Such settlements that are driven by litigation costs do nothing to vindicate the purposes of the substantive statutes or common-law causes of action at issue and merely represent a wealth transfer to opportunistic plaintiffs (and their lawyers). Rule 23 was never intended to create such incentives or to facilitate such outcomes, yet this will be the unavoidable consequence of the standards established by the court of appeals.[5] Accordingly, the court of appeals' approach is fundamentally flawed and warrants this Court's review.

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[5] The increased prospect of "wealth transfer" settlements created by the decision below is particularly unwelcome, but also particularly likely, in the current economic downturn. *See* Cornerstone Research, *Securities Class Action Filings, 2008: A Year in Review* 2 (2009), *available at* http://securities.stanford.edu/clearinghouse_research/2008_YIR/20090106_YIR08_Full_Report.pdf (noting that "[f]ederal securities class action activity in 2008 was dominated by a wave of litigation against firms in the financial services sector").

III. THE CIRCUIT CONFLICTS AT ISSUE FALL SQUARELY WITHIN THE COURT'S TRADITIONAL DUTY TO ENSURE UNIFORMITY ON ISSUES OF FEDERAL PROCEDURE AND, IF LEFT UNRESOLVED, WILL INCREASE FORUM-SHOPPING.

Even aside from the flaws in the court of appeals' holdings, this Court's intervention is necessary to remedy the current lack of uniformity on potentially dispositive issues of class action procedure. It goes without saying that standards for federal procedure should be uniform so that parties do not obtain disparate outcomes merely by virtue of geography. Indeed, the very purpose of the Federal Rules of Civil Procedure was to create a "'single uniform system of procedure.'" Erwin Chemerinsky & Barry Friedman, *The Fragmentation of Federal Rules*, 46 Mercer L. Rev. 757, 780 (1995) (quoting Charles E. Clark, *The Challenge of a New Federal Civil Procedure*, 20 Cornell L.Q. 443, 448 (1935)). Congress charged this Court with the responsibility to "prescribe uniform Rules to govern the 'practice and procedure' of the federal district courts and courts of appeals." *Burlington N. R.R.* v. *Woods*, 480 U.S. 1, 5 n.3 (1987) (quoting 28 U.S.C. § 2072). Accordingly, parties deserve uniform interpretation and application of Rule 23; only this Court can ensure that it is applied consistently.

Moreover, variant practices among federal courts on important issues of procedure, like the Rule 23 issues presented here, inevitably give rise to forum shopping. When procedural rules differ among available forums, plaintiffs will select the forum that they perceive to be the most favorable to them. Forum shopping is undesirable because it results in

unfairness, as well as inefficiencies from added costs to the parties and courts. Chemerinsky & Friedman, *supra* at 782-83; see also James D. Cox, Randall S. Thomas & Lynn Bai, *Do Differences in Pleading Standards Cause Forum Shopping in Securities Class Actions?: Doctrinal and Empirical Analyses*, 2009 Wis. L. Rev. 421, 452 (2009) (forum-shopping "undermines substantive law, overburdens jurisdictions with the most plaintiff-friendly approach, tends to place the suit in a locale that is removed from the source of the contest so that the litigants' expenses are greater, and perpetuates a negative perception of the fairness of the legal system").

The lack of uniformity here regarding whether uninjured plaintiffs can be included in class actions and who has the burden to establish the appropriateness of class certification provides a strong incentive for plaintiffs to choose to litigate in the Seventh Circuit. As noted, class action certification is a high-stakes issue that effectively resolves many cases before they ever reach the merits. Given the central importance of class certification, plaintiffs will seek out and be drawn to jurisdictions with procedural rules that favor and facilitate class certification. See Cox, Thomas & Bai, *supra* at 439 (noting that the liberal venue provisions of the federal securities laws provide plaintiffs' counsel with "essentially unlimited choices of where to file").

The standards adopted by the Seventh Circuit in the decision below do precisely that. The court of appeals' inversion of the burden of proof allows plaintiffs to obtain class certification more readily and its approval of classes that contain uninjured plaintiffs places enormous pressure on defendants to settle. This gives plaintiffs a clear incentive to file

putative class actions in district courts in the Seventh Circuit. Indeed, as noted, class action plaintiffs and their attorneys are already touting the Seventh Circuit's plaintiff-friendly rules. Accordingly, if left uncorrected, the decision below will result in forum-shopping that will serve no useful purpose and that will unfairly force defendants to settle with plaintiffs who have suffered no injury – or even benefited – at their hands. Because the decision below presents at least two fundamental and recurring issues concerning the proper interpretation of Rule 23 that will unfairly distort the litigation process in large class actions, the Court should grant certiorari.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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